



SONI TSO Governance Consultation Proposals

2 April 2021



About the Utility Regulator

The Utility Regulator is the independent non-ministerial government department responsible for regulating Northern Ireland's electricity, gas, water and sewerage industries, to promote the short and long-term interests of consumers.

We are not a policy-making department of government, but we make sure that the energy and water utility industries in Northern Ireland are regulated and developed within ministerial policy as set out in our statutory duties.

We are governed by a Board of Directors and are accountable to the Northern Ireland Assembly through financial and annual reporting obligations.

We are based at Queens House in the centre of Belfast. The Chief Executive leads a management team of directors representing each of the key functional areas in the organisation: Corporate Affairs, Markets and Networks. The staff team includes economists, engineers, accountants, utility specialists, legal advisors and administration professionals.



Our mission

To protect the short- and long-term interests of consumers of electricity, gas and water.



Our vision

To ensure value and sustainability in energy and water.



Our values

- Be a best practice regulator: transparent, consistent, proportionate, accountable and targeted.
- Be professional – listening, explaining and acting with integrity.
- Be a collaborative, co-operative and learning team.
- Be motivated and empowered to make a difference.



Abstract

We published a Call for Evidence in relation to SONI TSO's governance arrangements in July 2019. We sought the views of all interested stakeholders as to any issues that may arise from the current SONI TSO governance arrangements in the light of recent, and the likely future, industry developments. The responses we received have assisted us in identifying whether there are any issues with SONI TSO's current governance arrangements and (if so) in understanding what steps may be needed to address them. Consequently, this paper sets out for consultation four options for changes to SONI TSO's governance arrangements.

We have asked for feedback on our conclusions and proposals through a series of questions set out in Section 6. It is then our intention to consider the feedback we receive from stakeholders and where justified propose licence amendments in respect of SONI's TSO licence which will be subject to further consultation.

Matters relating to SEMO are outside the scope of the governance review.

Audience

This document is likely to be of interest to; SONI, NIE Networks, electricity generators, electricity suppliers, government, consumers, consumer groups with an interest in the energy industry.

Consumer impact

Compared to SONI TSO's current governance, the options proposed in this paper are designed to better secure the protection of the interests of NI consumers and other stakeholders now and into the future. An initial cost benefit analysis for each option is set out in Section 6.



Contents

1.	Introduction.....	11
	Background	12
	The Role of UR	12
	SONI as TSO	14
	SONI as SEMO	15
	Structure of this document	17
2.	Aligning Objectives of the Shareholder and Consumer	18
3.	A Vision of Good Governance	22
	Context for good governance of SONI TSO	22
	Developments in UK Corporate Governance.....	23
	Vision for good governance in achieving a trusted relationship.....	24
	SONI's current governance arrangements	25
	SONI Ltd. Board composition and duties	25
	Resources in SONI to support the Board	26
	Other elements of the governance framework.....	27
	Does SONI meet the vision for good governance?	28
4.	Issues raised with the regulation and governance of SONI	
	TSO in the CfE responses.....	29
	The Evidence of Harm or Potential Harm	29
	Inappropriately higher prices.....	30
	Misalignment in network development	33
	Barriers to Competition.....	33
	SONI TSO Governance: potential for conflict between aims of shareholders and consumers	35
	Scope of Decision Making.....	36
	Cost and Benefit Allocation	38
	Prioritisation of the Republic of Ireland's economy.....	38
5.	Remedies available through existing regulatory framework	40
	Measures in the current SONI TSO licence	40
	Prices	40
	Network development.....	42
	Competition	44
	Initial Conclusions	45
6.	Remedies Based on Changes to SONI TSO Governance.....	48



Proposed changes to governance	49
Summary of Consultation Options	52
Composition of the SONI Board	55
Duties of SONI Board and Matters Reserved	60
Board Committees	63
Independence of SONI TSO Management	64
Case Study	67
Other Governance Change Proposals	69
Future review of governance effectiveness	72
Cost / benefit of proposals	73
Questions	81
7. Assessment of the Options.....	85
8. Responding to this consultation and next steps.....	91
Process and timetable	91
How to respond.....	91
Confidentiality	91
Annex 1: Summary of non-confidential responses from Call for Evidence and UR response	93
Overview of non-confidential responses received and UR response.....	93
Annex 2: Summary of SONI's current governance arrangements .	94
Purpose of this annex.....	94
SONI Board composition and duties	95
Resources in SONI to support the Board	97
Other elements of governance framework, including to promote transparency	99
Annex 3: Regulatory Precedents.....	102
European Directives	102
Current SONI Licence Conditions	103
Treatment of the Electricity System Operator (ESO) in GB	103
OFWAT: Board leadership, transparency and governance principles	105
Regulation of National Grid in the USA.....	106
Governance of Elia in Belgium	108
Governance of NIE Network Businesses (Northern Ireland)	108
Whistleblowing Precedents	109
Annex 4: SONI Upfront service expectations	113

Executive Summary

Background to our Governance review

The structure of the electricity transmission sector in Northern Ireland (NI) has undergone significant change since the System Operator of Northern Ireland (SONI) was acquired by EirGrid in 2009. Moreover, in the next few years the transmission system is expected to play a critical role in the development of the power sector as NI, in keeping with other countries, moves to a low carbon economy.

A review of SONI's governance arrangements has not been undertaken since its acquisition by EirGrid. Our review was signalled during the project to develop the new wholesale electricity market, the Integrated Single Electricity Market (ISEM). Ultimately, our review has been undertaken to ensure that SONI is being governed in the best interests of NI consumers. Moreover, it is focused on ensuring that SONI is able to adequately address the requirements of an independent Transmission System Operator (TSO). This entails SONI acting as a trusted advisor in the provision of objective and transparent advice to government, the regulator and users in order to achieve a low carbon economy.

On 9 July 2019, we initiated this review through a Call for Evidence and sought views from all interested stakeholders on a range of issues.

When we initiated the review, the aims were to:

- ensure SONI's licence conditions on independence are clear and fit for purpose;
- determine how SONI's governance structures work in practice;
- identify whether these arrangements pose any risk of harm to NI consumers that requires additional regulation;
- see if additional measures (e.g. licence modifications) are needed, identify and develop the proportionate measures needed;
- ensure that governance arrangements are fit for purpose into the future energy transition and do not place limits on the effective regulatory discretion of the Utility Regulator (UR) or policy discretion of the UK Government and NI Executive; and,
- ensure transparency and confidence in the arrangements among market participants in NI.

In response to that Call for Evidence we received many submissions from a wide range of stakeholders, some of which were anonymous, with many signalling a requirement that their views remain confidential. We also received two responses from SONI, the first in reply to the initial Call for Evidence and the second as a response to additional questions we posed to SONI covering gaps in its initial submission and also seeking further information on areas raised by responders.

Our call for evidence findings

We have reviewed and analysed all of the responses received. We have assessed ‘what good looks like’ in the practices, processes, behaviours and accountability we should expect from an independent TSO. This assessment incorporated the statutory obligations on both UR and TSO as well as the activities and behaviours set out and consulted upon in our price control consultation¹. We have also considered other sources of good governance as might be deemed relevant including initiatives adopted by other regulators and the principles of the UK Corporate Governance Code (UKCGC).

We recognise that there is a balance to be struck between oversight by the parent company (EirGrid plc) and the autonomy needed by the subsidiary. However, in SONI's case the subsidiary is also a regulated TSO² and therefore the interface with the regulator who safeguards the interests of consumers is particularly important. Our vision for good governance is based on achieving a trusted relationship with SONI. This means that we want SONI to play a proactive role in the implementation of NI government policy, provide clear, accurate, and timely information to us and other stakeholders. It also means that we expect that SONI ensures compliance with licence conditions and other legal obligations. Where SONI must also discharge responsibility for defined all-island matters with EirGrid, SONI TSO's governance should enable:

- both TSOs to work together collaboratively but as equal partners representing their own consumers;
- collaboration on the basis of a formal agreement with clear rules;
- mechanisms to resolve disputes between the TSOs; and
- decision making which records how the balance between the interests of the two different sets of consumers had been achieved, in particular where they are not aligned.

Our Call for Evidence has established the nature of SONI's current governance arrangements and the level of autonomy the company has in its relationship with EirGrid plc. We conclude that the management and oversight of SONI TSO licence responsibilities are effectively discharged by EirGrid plc, and not by SONI Ltd. In addition, the integrated governance structures of the EirGrid group are not designed to enable SONI to act as an equal partner, nor even to be perceived as an equal partner with its own guiding mind. Moreover, there is no robust set of rules to govern collaboration between the TSOs – these are either missing or not working for

¹ <https://www.uregni.gov.uk/consultations/soni-price-control-2020-2025-draft-determination-consultation>

² Matters relating to SEMO are outside the scope of the governance review.

reasons explained in Section 3. Overall, we therefore consider that SONI's present governance arrangements do not meet our vision for good governance.

During the Call for Evidence a range of stakeholder concerns were identified. Several of the observations reveal a potential, and increasing potential, for harm to result from the current operating and governance arrangements, the risks of which are not sufficiently mitigated within the current licence conditions. Overarching concerns appear in the responses about a lack of transparency and accountability. More specific concerns can be summarised as follows:

- management and decision making in respect of TSO activities are increasingly performed on an shared management basis, potentially to the detriment of NI consumers;
- objectives of management and staff are predominantly aligned with the shareholder, without sufficient balance in respect of NI consumers;
- plans, policies, cost and benefit allocations are not wholly transparent or approved by an effective SONI Board;
- the lack of a System Operator Agreement (SOA) to transparently govern collaboration between the two TSOs. SONI states this agreement has been 'internalised' by the shared operating model employed across the EirGrid group; and,
- the lack of a current 'Condition 12' compliance plan on the independence of the TSO, which diminishes the transparency and accountability of SONI.

We are concerned that the above areas could potentially give rise to:

- **inappropriately higher prices for NI consumers**, particularly through the obfuscation of information including the increasing levels of inter-company recharges disclosed within the SONI Regulatory Accounts. The price control process to set prices is predominantly based upon historic cost trends, reflecting challenges in finding a robust and efficient comparator for SONI. Hence, there is a concern over the absence of any adequate shareholder incentive to make cost information transparent to the regulator compounded by the lack of an effective SONI management and Board to oversee and approve those costs;
- **misalignment of NI policy and the SONI approach to network development** through a 'one-size fits all' approach to investment and operational decision-making, potentially agreed in a shared management model and decisions therefore risk being taken for the benefit of shareholders and not NI consumers specifically. This also includes the risk that NI network and user differences are not sufficiently encapsulated within decision-making;

and,

- **barriers to competition** whereby, again, the shared management and operating model employed across EirGrid and SONI risks a 'one-size fits all approach' which may not properly account for differences in developing and operating the NI network. This is significant - both in the procurement of system services, and system analysis and planning.

A number of respondents expressed a range of concerns with the ownership of SONI arising in particular from the fact that EirGrid plc is owned by the Government of Ireland. We are not persuaded that there is evidence available in support of these concerns or which establishes harm or potential harm that arises from the ultimate ownership of SONI.

Many of the concerns expressed by stakeholders resulted from the fact that the two TSO Licensees are operated under a shared management and resource model compounded by the lack of transparency in key areas. These concerns would not exist if the governance of the two licensed entities was sufficiently separate.

Some stakeholders wanted to retain the potential for synergies and cost efficiencies for both consumers in the Republic of Ireland and NI and saw the shared management and operating model as beneficial in this context. We understand these views but the opportunities from a shared management and operating model need to be balanced by protections afforded to both consumers in NI and Republic of Ireland.

This balance and the need for greater trust and transparency has been the subject of much change in the regulatory environment, not just within the electricity sector and NI but with regulatory frameworks in other utilities and across other jurisdictions. In looking to better develop trust and transparency, and establish an appropriate balance of incentives across the different stakeholders, regulators have implemented a number of licence changes with the intention of:

- obtaining greater levels of information detail and more prescription of outcomes to be achieved by regulated utilities. We currently employ each of these licence requirements but note that whilst more intrusive regulation may deliver greater transparency, it also risks more allocation of responsibility to regulators and less trust and accountability within regulated businesses;
- increasing effective competition and separating activities across the value chain where this is achievable. To ensure effective competition, business separation rules and reporting are introduced to avoid market distortion from shared ownership ; and
- greater independence of the Board and management with the potential for balanced objectives between shareholders and consumers better reflecting the needs of relevant consumers and users, as well as improved trust and

accountability. The level and scale of independence of resources needs to be proportionate, and considered against the potential for increased costs and reduced synergies.

Our principal objective is to protect the interests of both current and future consumers in NI. This is concerned not only with ensuring the absence of harm³ but with optimising benefits to consumers by actively promoting improved outcomes over the long-term. Consequently, we do not need to identify a source of existing harm before we can act. This aligns with our statutory duty to protect the short and long-term interests of NI consumers.

Our proposals for SONI Governance – four options for consultation

Following the analysis of the information received through the call for evidence and all other relevant information, we consider that the current governance structure of SONI TSO is inadequate to ensure the protection of the interests of NI consumers over the long-term. This situation also poses too many risks for those consumers. In order to mitigate these risks and protect the interests of NI consumers, we have identified four options for consideration and consultation as outlined in the figure below and explained in greater detail in Section 6. The changes we propose are based upon best practice initiatives employed elsewhere by regulators to remedy similar concerns. They will also ensure SONI meets our vision for good governance, including by introducing protections into the SONI TSO licence in a manner that preserves the collaboration between the two TSOs which is fundamental to the SEM.

In regards to SONI's Board, the risks identified do not arise from the individuals on the Board but arise from the structure of the Board and whether it will promote good governance compared to one structured along the lines envisaged by the UKCGC.

These options are similar to Options 4 and 5 set out in Section 7 of the Call for Evidence. All the responses which expressed a preference for a particular option or options favoured Options 4 and 5.

All of the options are designed to ensure that SONI and EirGrid deliver their SEM all-island TSO functions as equal partners representing their own consumers. Matters relating to SEMO are outside the scope of this governance review. Whether something is a SEM matter is a question for the SEM Committee (SEMC). SEMC is aware of UR's review into the SONI governance arrangements and has to date decided that the matter is jurisdictional in nature and therefore falls under the remit of UR, not SEMC. We will keep the SEMC informed as the governance review progresses.

³ Such as actual consumer detriment or failure to comply with a legal obligation.

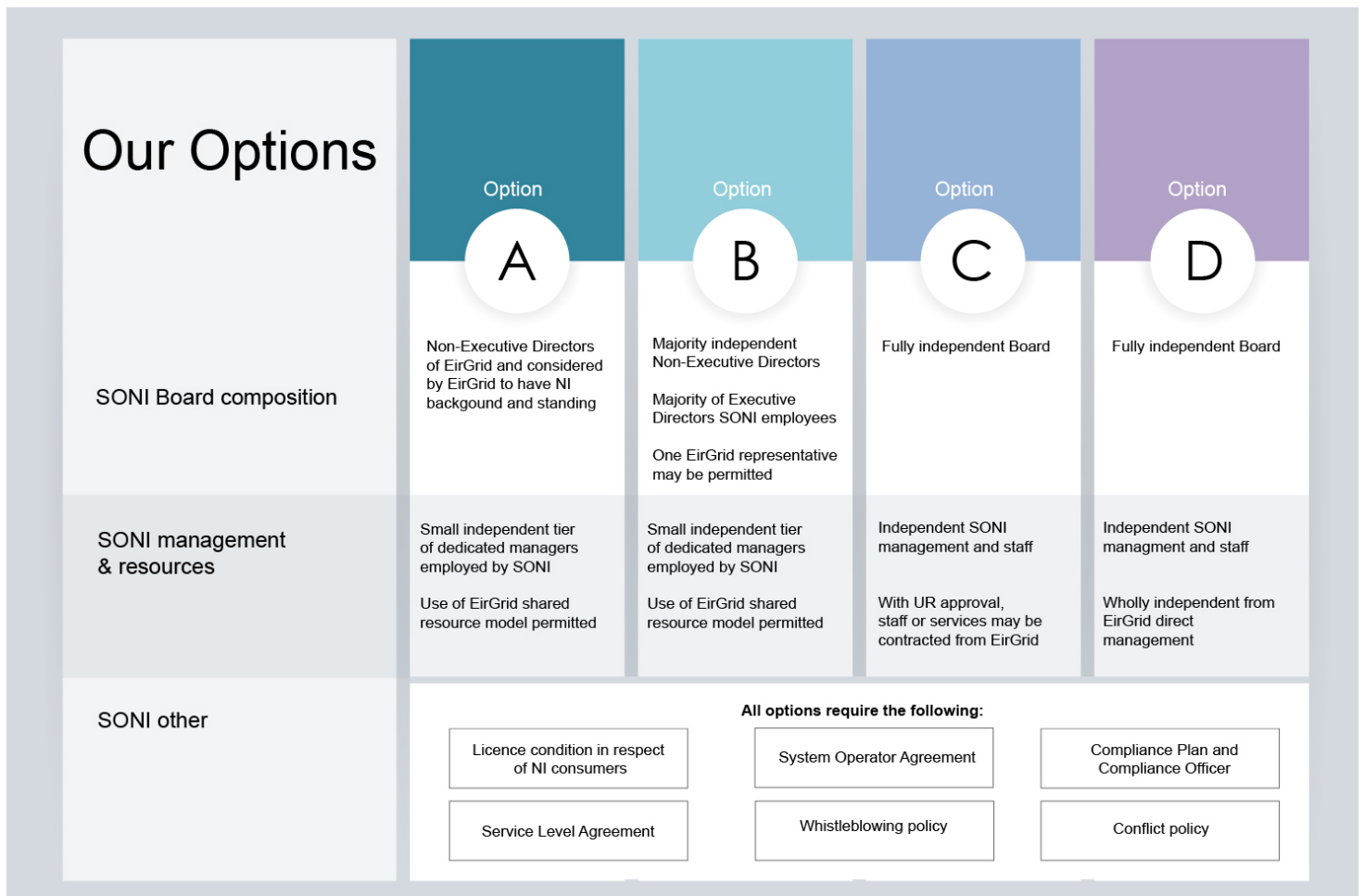


Figure 1: outline of consultation options

Our provisional view at this stage is to rule out Option A because it does not go far enough to meet our vision for SONI governance and provide sufficient protection for NI consumers. Option D, while a viable option to address the risks identified, could potentially remove all of the efficiencies that could be gained between the TSOs.

Provisionally, our preferred options are therefore Options B and C. Options B and C are likely to represent the most proportionate interventions considering the evidence we have received to date. They will provide effective transparency and accountability by SONI for the delivery of its TSO obligations. They each allow SONI to maintain scope to deliver any synergies and related efficiencies which may arise from SONI's position in the EirGrid group while allowing better alignment of the commercial interests of SONI's shareholder with the interests of NI consumers. Crucially, both Options B and C will also ensure increased transparency compared to the current operating arrangements.

Option C goes further than B by expanding the scope of the dedicated management team reporting to the SONI Managing Director (MD) under a fully independent Board. It also specifies that resource below the management level is dedicated to

SONI. SONI management and staff would be employed by SONI and report to the SONI Board. However, Option C would allow an independent SONI Board to make an evidenced case to UR to permit sharing of resources with EirGrid. This would likely only be permitted in C where it would deliver tangible efficiencies for the NI consumer and/or result in SONI being demonstrably more effective than would otherwise be the case, whilst maintaining independent SONI decision making and accountability.

Further steps could be taken, as illustrated by Option D. The measures in the NIE Networks transmission and distribution licences are similar to those proposed in Option D.

In Section 6, we have asked for feedback on our conclusions and proposals through a series of questions. It is then our intention to consider the feedback we receive from stakeholders and where justified, propose licence amendments in respect of SONI's TSO licence that will be subject to further consultation. The next steps in the governance review are set out in Section 8.

We will keep any new obligations agreed at the outcome of this consultation under constant review, and SONI will be required to demonstrate its compliance with any new obligations, and that it is an effective partner to EirGrid TSO in all-island TSO decision making. Given the importance of ensuring SONI TSO as a trusted advisor in the ongoing transition to a low carbon economy, we believe it appropriate to undertake a formal review of the effectiveness of SONI TSO governance two years after any new measures have been implemented. The aim is that such a review is concluded in advance of the next price control process. This review could recommend further changes, including the need for greater independence if found necessary.

1. Introduction

1.1 In July 2019, we initiated a review of the governance arrangements of the electricity transmission system operator of NI, SONI, to ensure that the company is, and will continue to be, fit for purpose in securing the protection of the interests of consumers. This review started with the publication of 'A Call for Evidence' (CfE) seeking views of all interested stakeholders as to any issues that may arise from the current SONI TSO governance arrangements in the light of recent, and likely future industry developments.

1.2 The structure of the electricity transmission sector in NI has undergone significant change since the SEM was implemented in 2007 and SONI was acquired by EirGrid in 2009. At that time a number of amendments were made to both the Licences of SONI and EirGrid and changes made to the Corporate Governance of EirGrid to better protect consumers across Ireland and NI. A review of SONI TSO's governance arrangements has not been undertaken since its acquisition and now more than ever, there is a need for a regulatory relationship between UR and SONI TSO which is both trusted and drives confidence.

1.3 The regulatory arrangements framework for utilities acknowledges that utility companies will focus on the interests of their shareholders, with regulators having a role to ensure these shareholder interests are balanced with those of consumers. Regulators achieve this through a variety of means, including approving plans to develop utility networks, limiting the prices that utilities can charge and establishing frameworks for competition between utility companies. These arrangements are each set out within the relevant licence.

1.4 The balance between consumer and shareholder interests has proved challenging to maintain across many utilities and jurisdictions, leading to greater informational transparency and changes of governance. For example, the governance of GB water companies has recently been amended by OFWAT, with amendments including licence objectives on the board to balance the interest of consumers with those of shareholders.

1.5 The regulatory challenges for electricity are, when compared to those for water, further complicated by structural differences and the change in the industry paradigm arising from moves to a Lower Carbon Economy. This informs an evolving energy policy bringing different types of generation (e.g. wind and solar) and demand (e.g. heat pumps and e-vehicles) onto the system. This, in turn, creates new challenges both for the optimal development of networks and for how generation and demand are controlled to maintain stable and secure electricity supplies. To navigate these changes in a way that balances consumer and shareholder needs, regulators and users need support and advice from those with detailed and impartial understanding of the development and operation of power systems. Ideally, this trusted advisor will be the System Operator (SONI for Northern Ireland) which has

hands-on experience of dealing with those challenges on a day-to-day basis.

1.6 The rest of this paper explores a number of issues in the balance of incentives between those of a shared management and resource model, and the interests of NI consumers specifically. We also discuss how similar issues have been addressed elsewhere. We then consider how these issues may best be remedied to get closer to SONI TSO being able to fulfil the trusted advisor role necessary for the optimal transition to a Low Carbon economy and better protect the interests of NI consumers.

Background

1.7 This review was signalled during the implementation process for ISEM which confirmed that UR would review the governance of SONI TSO to ensure that it continues to adequately address the requirements of an independent TSO for NI. The process was initiated in July 2019, with the publication of a CfE seeking views of all interested stakeholders as to any issues that may arise from the current SONI TSO governance arrangements in the light of recent, and likely future industry developments.

1.8 We have now reviewed responses from many stakeholders, both individuals and corporate bodies, some of which were anonymous. We have also received submissions from SONI, both in respect of the initial CfE and in respect of a follow-up document where we made specific enquires of SONI with regards that initial submission. This document therefore focuses on the responses we received to our CfE.

The Role of UR

1.9 The role of UR is determined under legislation and its statutory principal objective in relation to electricity matters is:

1.10 “To protect the interests of electricity consumers in Northern Ireland, wherever appropriate by promoting effective competition between persons engaged in or in commercial activities connected with the generation, transmission or supply of electricity.”

1.11 UR is a non-ministerial government department, accountable to the NI Assembly.

1.12 In carrying out its functions, UR should act in the manner best calculated to further the principal objective, having regard to:

- The need to secure that all reasonable demands in Northern Ireland or Ireland for electricity are met; and

- The need to secure that licence holders are able to finance the activities which are the subject of obligations imposed under NI energy law.

1.13 UR is required to carry out its respective electricity functions in the manner which it considers is best calculated:

- To promote the efficient use of electricity and efficiency and economy on the part of persons authorised by licences or exemptions to supply, distribute or participate in the transmission of electricity;
- To protect the public from dangers arising from the generation, transmission, distribution or supply of electricity;
- To secure a diverse, viable and environmentally sustainable long-term energy supply;
- To promote research into, and the development and use of, new techniques by or on behalf of persons authorised by a licence to generate, supply, distribute or participate in the transmission of electricity; and
- To secure the establishment and maintenance of machinery for promoting the health and safety of persons employed in the generation, transmission, distribution or supply of electricity.

1.14 In performing the above duties, regard shall also be had to the interests of groups of vulnerable consumers in NI, comprising the disabled and chronically sick, pensioners, low income consumers and residents of rural areas.

1.15 In carrying out its electricity functions, UR must not discriminate between persons whose activities include generating, supplying or transmitting electricity.

1.16 For the purposes of these obligations, all references to “consumers” include both existing and future consumers.

1.17 UR undertakes these obligations through the granting and ongoing development of the licensing regime under which SONI operates.

1.18 This document therefore focuses on the responses we received to our CfE considering whether the current governance arrangements still adequately protect the interests of consumers:

- If the responses evidence behaviours and good practice governance arrangements by SONI that optimise benefits to consumers;

- If (and if so, how) those responses evidence harm (be that actual or potential) to NI consumers of electricity;
- The extent to which these areas of harm can be managed within the existing governance and licence regime for SONI;
- Potential remedies (including changes to SONI TSO governance) to address outstanding areas of harm; and
- Potential changes to optimise benefits to consumers.

SONI as TSO

1.19 SONI is licensed under Article 10 of The Electricity (Northern Ireland) Order 1992 as the Transmission System Operator (TSO) for NI. As TSO, SONI has general duties under the legislation to:

- Ensure the development and maintenance of an efficient, co-ordinated and economical system of electricity transmission;
- Contribute to security of supply through adequate transmission capacity and system reliability; and
- Facilitate competition in the supply and generation of electricity.

1.20 SONI's licence obliges it to undertake a number of activities, collectively referred to as the Transmission System Operator Business, which include:

- Planning and operating, and co-ordinating and directing the flow of electricity onto and over, the transmission system;
- Maintaining security standards;
- Operating the balancing market;
- Procuring System Support Services (including DS3 services); and
- Operating the Capacity Market.

1.21 SONI is thus responsible for carrying out functions that are at the core of the NI electricity system and vital to the NI economy as a whole.

1.22 In delivering many of these functions SONI must interface with EirGrid TSO and the terms of this interaction are set out in the SOA. The SOA defines areas of coordination ('interface obligations') between SONI and EirGrid. Within these areas of interface each individual TSO has their jurisdictional responsibilities and the interfaces manage how they 'work with one and other', 'liaise', 'agree jointly' and 'co-

ordinate'. The SOA does not imply that the TSOs act as one entity in the activities it governs, unlike with the Market Operator which is a contractual joint venture between SONI and EirGrid and is discussed below.

1.23 It is clear from the construct and governance of the SOA, in particular the existence of a formal dispute resolution process, that the TSOs should operate as independent entities at either side of the interfaces and the representatives on the Steering Committee and the Joint Management Committee are to come from two independent entities. The existence and operation of such an agreement also provides transparency to users as to accountability and process.

SONI as SEMO

1.24 SONI holds a second licence: which licenses SONI as the SEM Operator (SEMO). The SEM Operator's duties in the legislation are limited to those covered by the SEM trading and settlement code. In the SEMO Licence, the functions of the 'Market Operator Activity' and 'Nominated Electricity Market Operator (NEMO) Activity' are defined as follows:

Market Operator Activity:

- Administration and maintenance of the 'Single Electricity Trading and Settlement Code' (the Code) which includes:
 - ◆ Setting out the terms of the trading and settlement arrangements for the sale and purchase of wholesale electricity in the Balancing Market; and
 - ◆ In conjunction with the Capacity Market Code, setting out the settlement arrangements for the Capacity Market.
- Facilitation of modifications to the code under modifications procedures (ultimate approval by the Regulatory Authorities);
- Operation and maintenance of the SEM Trading and Settlement System under the Code;
- Carrying out market operator obligations under the Code; and
- Acting as 'Agent of Last Resort'.

Nominated Electricity Market Operator (NEMO) Activity:

- Performance of the day-ahead and intraday market coupling arrangements which includes (as defined by the CACM Regulation);
- Operation of the day ahead market; and

- Operation of the intraday market.

1.25 The structure and governance of the MO is very different to that of the TSOs, working in conjunction under the SOA. This reflects the fact that SEMO is a contractual joint venture (CJV) between EirGrid and SONI.

1.26 While there are two MO licences issued to SONI in NI and EirGrid in ROI, the CJV 'SEMO' has its own resources separate to the TSO's. SEMO has a separate price control, which is distinct from the SONI TSO Price Control in NI and the EirGrid TSO Price Control in the Republic of Ireland. There is a Market Operator Agreement (MOA), but this is not an interface agreement as per the SOA.

1.27 The MOA governance structure is also quite different than that of the SOA, particularly given that SEMO is a CJV with its own resources. Specifically, the SEMO governance structure comprises a Governing Committee and a General Manager. The functions of the Governing Committee are as follows:

- Appointment and replacement of the General Manager;
- Approval of the submission to the Regulatory Authorities for the SEMO price control;
- Approval of the SEMO budget annually (all resources including staff);
- Approval of any matters outside of the budget (including staff recruitment outside of the budget); and
- Determining (and notifying where appropriate) a Force Majeure under the MOA or the Trading and Settlement Code.

1.28 The functions of the Governing Committee clearly show how different the structure of the MOA is to the SOA in both form and effect. It follows that SONI's MO and NEMO functions are deliberately designed to be integrated with EirGrid's MO and NEMO functions.

1.29 Matters relating to SEMO are outside of the scope of the governance review. Matters relating to SEMO are separately regulated under different licences. To the extent that any responses received as part of the governance review relate to matters that fall within SEMC's jurisdiction, we propose to pass any responses pertaining to SEMO gathered to SEMC.

Structure of this document

1.30 The structure of this document is as follows:

- How the objectives of companies and regulators may align or conflict (Section 2)
- A vision of good governance (Section 3)
- Consideration of the issues raised in the responses to the CfE (Section 4)
- Remedies available through existing regulations (Section 5)
- Proposed further remedies (Section 6)
- Assessment of options (Section 7)
- Responding to this consultation and next steps (Section 8)
- Annexes:
 - ◆ Summary of non-confidential responses to the Call for Evidence and UR response
 - ◆ Summary of SONI TSO governance arrangements
 - ◆ Regulatory governance precedents
 - ◆ UR service expectations for SONI TSO

2. Aligning Objectives of the Shareholder and Consumer

2.1 It has long been recognised that the interests of shareholder owned utilities are not entirely aligned with those of the consumers they serve. These companies are set up to serve the interests of their shareholders who, in turn appoint the board.

2.2 The board of any company is subject to fiduciary objectives set out (for UK Companies) in The Companies Act 2006, which includes the duty to promote the success of the company for the benefit of its members as a whole. That obligation includes having regard to the need to foster relationships with suppliers, customers and others and the impact the company's operations has on the community and environment. However, the extent to which these obligations explicitly align with those of consumers is tenuous for monopoly utility businesses extending to the specific requirements detailed within their respective licences. For monopoly utility businesses, a company can be financially successful without giving much consideration to customer benefits. This means the duty to consider those needs is, at best, weak for directors of those monopoly companies.

2.3 OFGEM have acknowledged issues with the alignment of shareholder and consumer objectives in their recent consultation paper on GB System Operation⁴. This notes that System Operators have a “limited appetite for risk taking [that] may prevent proactive leadership in complex areas”. This is driven (in part) by a “reputational risk” that external stakeholders may take issue with the System Operator's view on how the operation and governance of the energy system should evolve to meet new challenges – such as those arising from the transition to a Low Carbon economy. We note that those external stakeholder views may, for a number reasons, differ between stakeholder types (legacy generators, renewable generators, load managers etc.) as well as between stakeholders in NI and the Republic of Ireland.

2.4 In recognition of this weak alignment of objectives, a number of measures have been established by policy makers to protect the interests of consumers:

- **Competition:** has been introduced, allowing customers to choose providers that align with their interests (be that on the basis of cost, customer service, green credentials, or another consumer interest);
- **Minimise conflicts across the value chain:** potential conflicts of interest arise where a company, by virtue of its role in the utility value chain, can influence the competitive outcome elsewhere in that value

⁴ Review of GB energy System Operation, Ofgem, 25 January 2021

chain. To mitigate such conflicts of interest, companies that carry out such influential roles are precluded from having a material interest in the relevant competitive areas of the value chain. For example, this applies to:

- ◆ **System Operators:** as energy utilities with significant influence over the outcome of competition between producers;
 - ◆ **Network Companies:** Competitive utility companies access their market through a physical network (e.g. wires or pipes). How this network is developed can significantly impact the ability of specific companies to access their market; and
 - ◆ **Market Operators:** administer elements of competitive markets – determining payments to be made to or by companies that compete in those markets.
- **Sector Regulator:** It is recognised that the above measures, on their own, are insufficient to fully ensure an appropriate balance between the interests of consumers and those of shareholders. Sector regulators have been established with the explicit duties and powers aimed to correct this balance. For example:
 - ◆ **Monopoly company revenues:** Where companies have market power such that competition does not fully constrain the prices they charge, sector regulators limit the prices charged to a level consistent with the investment needs of that company; and
 - ◆ **Market failure:** Regulators will monitor for areas where markets and competition fail to act in the interest of consumers or society as a whole. Where possible, they will remedy such market failures.

2.5 The above framework has evolved and been refined with experience, recognising a number of issues:

- **Information disparity:** In carrying out its role, a regulator is at an information disadvantage in terms of understanding the intricacies of the companies it regulates. This is true for all utility activities. This disparity has led regulators to introduce more specific outcomes expected of companies and require greater levels of detail in the information they demand of companies they regulate.
- **Increasing trust:** Regulators and regulated companies have driven or proposed changes in governance to aid trust and stakeholder

influence. As an example, OFWAT required changes to the governance of GB water companies following damaged trust in the sector after the corporate behaviour of some companies and significant service failures. These changes included:

- ◆ Requiring the company's board to have a majority of Non-Executive Directors; and
 - ◆ Introducing explicit obligations such that the board balance the interests of those it serves⁵ and to increase transparency.
- **Changing industry paradigm:** Regulators are typically managing utilities where the underlying utility infrastructure and technology is relatively stable, with this stability helping to correct for the information disparity. The underlying paradigm of the electricity industry is now unstable, with the industry having a leading role in moves to a low carbon economy. This brings new challenges in terms of accommodating renewable and distributed generation, along with new types of load and load response as heating and transport move to electricity.

The regulatory arrangements for electricity may need to change to ensure that the interests of consumers are optimised throughout this paradigm change. Given the highly technical nature of the industry, regulators will need analysis and support from those dealing with the challenges of the paradigm shift on a daily basis. This has led to changes to the governance of the electricity system operator (ESO) in GB, including:

- ◆ Separating the system operator function from the ownership of transmission assets (wires, transformers, switches, etc). This potentially further reduces or removes any conflict of interest (perceived or otherwise) the System Operator may have in favouring an infrastructure supported system of bulk transport of electricity over large distances, and so is more consistent with objective analysis for how low carbon generation can be accommodated.
- ◆ Establishing an independent board for the System Operator; and
- ◆ Further changes to GB System Operation are now being considered by OFGEM⁶, with one of their main findings

⁵ That is all stakeholders - including shareholders and customers

⁶ Review of GB energy System Operation, OFGEM, 25 January 2021

(Finding 2) being that “The System Operators are uniquely positioned to play a critical role in achieving net zero”

2.6 The framework set out above is illustrated through a number of specific precedents which are summarised in Annex 3:

- European Directives;
- Current SONI TSO Licence Conditions;
- Treatment of the Electricity System Operator (ESO) in GB;
- OFWAT: Board leadership, transparency and governance principles;
- Regulation of National Grid in the USA;
- Governance of Elia in Belgium; and
- Governance of NIE Network businesses.

3. A Vision of Good Governance

Context for good governance of SONI TSO

3.1 As part of the work to set UR's 2020-2025 price control for SONI TSO, we set out service expectations for SONI TSO (see Annex 4). These outlined our position on what a good TSO would do and/or achieve in each service area. These expectations are grounded in SONI TSO's statutory obligations in respect of NI consumers to:

- Develop and maintain an efficient, co-ordinated and economical network capable of meeting the long-term reasonable demands for the transmission of electricity;
- Contribute to Security of Supply through adequate capacity and reliability; and
- Facilitate competition in Supply and Generation.

3.2 A key strand of our expectations is that we believe SONI TSO should be taking a more whole system, collaborative and coordinated approach to working with various stakeholders, including NIE Networks. Therefore, in fulfilling its role as TSO, including its role as independent expert, we expect SONI TSO to:

- Seek to operate and develop the network in a way that best balances short term costs and longer-term needs for the benefit of NI consumers and users;
- Support users to make informed decisions through seeking and embracing their requirements with openness and transparency;
- Maintain efficient operations that benefit NI consumers in the short and long term;
- Operate and develop the network so as to meet reliability and capacity requirements in the short and longer term, meeting the needs of NI users; and
- Collaborate with parties across the whole of the network to improve competition, deliver innovation and minimise short and long term costs to the NI consumer.

3.3 Good governance will support the delivery of our service expectations for SONI TSO by helping SONI to drive appropriate behaviours for a regulated company remunerated by customers. In particular it will help SONI TSO build and maintain collaborative relationships with a wide range of stakeholders, including the

UR. These relationships will be successful and enduring if they are based on respect, trust and mutual benefit.

Developments in UK Corporate Governance

3.4 UK corporate governance has continued to evolve since the first version of the UK Corporate Governance Code (UKCGC) was published by the Cadbury Committee in 1992 in response to a number of governance failures. The basis of the current code is that “companies do not exist in isolation ... and to succeed in the long term ... they need to build and maintain successful relationships with a wide range of stakeholders. These relationships will be successful and enduring if they are based on respect, trust and mutual benefit. Accordingly, a company’s culture should promote integrity and openness, value diversity and be responsive to the views of shareholders and wider stakeholders.”

3.5 At the heart of the current UKCGC, dated 2018, is an updated set of principles, not a rigid set of rules that place a greater emphasis on relationships between companies, shareholders and other stakeholders and promote the importance of establishing a corporate culture that is aligned with the company purpose and strategy, promoting integrity and that values diversity. It is a requirement of those companies with “Premium Listing” that they report on how they have applied the code and it is seen as a basis of best practice governance more widely. Those principles cover the following areas:

- Board Leadership and company purpose;
- Division of responsibilities;
- Composition, succession and evaluation;
- Audit, risk and internal control; and
- Remuneration.

3.6 The CfE highlighted the UKCGC as a reference point for what good governance looks like. Whilst only a requirement on listed companies, we consider that any regulated utility that can demonstrate it is applying the principles of the UKCGC may be said to have reflected good corporate governance. In that regard we note that the UKCGC is not a rigid set of rules; instead it offers flexibility through the application of a set of principles and through ‘comply or explain’ provisions and supporting guidance.

3.7 In the CfE we requested respondents’ views on:

- Whether it is appropriate to apply the principles in the UKCGC to SONI, in whole or in part;

- The extent to which SONI could already be said to meet the principles contained in the UKCGC; and
- Whether the principles in the UKCGC, to the extent respondents consider they should apply, should be codified in the licence or could be implemented on a voluntary basis by SONI.

The responses to these questions are set out in Annex 1. We have been guided by the principles of the UKCGC when developing the options for consultation and therefore consider that it is not necessary at present to require SONI to implement the UKCGC by means of a licence obligation.

Vision for good governance in achieving a trusted relationship

3.8 UR recognises that when considering governance in any utility there is a balance to be struck between oversight by the parent and the autonomy needed by the subsidiary. However, in this case the subsidiary is also a regulated TSO and therefore the interface with the regulator who safeguards the interests of consumers is particularly important.

3.9 In addition, and reflecting that SONI is a regulated TSO, where SONI TSO is delivering for NI consumers its governance should encourage and enable it to:

- Play a proactive role in the implementation of NI government policy, e.g. energy transition;
- Provide clear, accurate, and timely information for the regulator and other stakeholders as appropriate; and
- Ensure compliance with licence conditions and other legal obligations.

3.10 Again, reflecting that SONI is a regulated TSO, but one which must also discharge responsibility for defined all-island matters with EirGrid, SONI TSO's governance should enable:

- Both TSOs to work together collaboratively but as equal partners representing their own consumers;
- Collaboration on the basis of a formal agreement with clear rules;
- Mechanisms to resolve disputes between the TSOs; and
- Decision making which records how the balance between the interests of the two different sets of customers had been struck, in particular where they are not aligned.

3.11 From the regulator's perspective, good governance incorporating all these elements has the advantage that the TSO's activities are transparent and so open to regulatory scrutiny. This allows any problems to be revealed over time and enabling the regulator, where necessary, to take corrective action. This layer of regulatory assurance further promotes trust and confidence in the TSO among stakeholders and market players. In the long term therefore, good governance will deliver the continued success and sustainability of the SONI TSO business.⁷

SONI's current governance arrangements

3.12 This section summarises the high-level features of SONI's governance, including the level of autonomy SONI Ltd. has in its relationship with its parent, EirGrid plc (which holds the licence for TSO activities in Ireland) and contrasts this with the vision for good governance set out above. A fuller summary of SONI's current governance arrangements is provided in Annex 2.

SONI Ltd. Board composition and duties

3.13 The composition of the SONI Board has changed significantly since UR commenced its governance review. At the time of writing, it comprises of three non-executive directors (NED's) and three executive directors. The most recent changes were made during the summer and early winter of 2020, and resulted in the appointment of three NEDs who are also on the EirGrid plc Board, one of whom also now chairs the SONI Board. Two of the appointments are persons considered by EirGrid to have significant standing in NI. This is a significant development compared to the previous SONI Board which was dominated by members of the EirGrid plc executive team. However, the fact that these appointees are also members of the EirGrid Board, is a circumstance which the UKCGC states is likely to impair or could appear to impair, their independence. For the same reason the revised Board's ability to manage any conflict of interest between the needs of NI and Irish consumers could also be impaired or could appear to be impaired.

3.14 We note that all SONI Ltd. Board members are appointed by EirGrid plc and there are no requirements in the SONI TSO licence as to the composition or independence of the Board. EirGrid plc could therefore change the board composition of SONI Ltd. at any time and in any way it chooses.

3.15 Turning to the duties of the SONI Board, information provided by SONI to UR indicates that the matters reserved to the SONI Board are very limited.⁸ A number of significant SONI functions are discharged either by the EirGrid plc Board or within the EirGrid Group integrated management structure, and the SONI Board has no formal role. More specifically the SONI Board:

⁷ This being a key aim of good corporate governance.

⁸ See Annex 2 for the list of matters reserved to the SONI Board.

- Does not set the strategic direction of the company;
- Does not monitor the development of or sign off the SONI business plan for the price control;
- Does not have a formal role in SONI risk management;
- Has no role in procurement decisions taken at group level and which incur cost for SONI;
- Has no role in signing off the Cost Allocation and Recharge Policy;
- Does not have responsibility for investment decision making for SONI which is carried out at a group level; and
- Has no role in approving commercial transactions with another group company – it can only approve transactions with an external third party and therefore, we infer, not transactions with EirGrid plc or other group companies.

3.16 From the information provided by SONI we conclude that the scope of authority of the SONI Board is extremely limited and therefore not designed to empower that Board to provide leadership for the company, set its strategic direction or provide oversight of the discharge of SONI's licence obligations.

Resources in SONI to support the Board

3.17 Whilst SONI has a small number of dedicated staff in respect of regulation, strategy and stakeholder engagement reporting to the SONI MD, it does not have a comprehensive dedicated management team or staff which is responsible for SONI TSO functions and which reports to the SONI Board. Instead EirGrid has adopted a 'cohesive all-island management structure' across the EirGrid group, under which there is one Executive team with the EirGrid Chief Executive Officer (CEO) at the head.

3.18 This means that the Executive Committee of EirGrid has management responsibility for all SONI TSO licence activities, including network operations, planning and company finances and operates these through an integrated management structure. SONI Managers and staff are pooled across the group, ultimately reporting to the EirGrid group CEO who in turn reports to the EirGrid plc Board. The SONI MD also reports to the group CEO. Grid development and investment decision making is also undertaken by group wide committees within the EirGrid Group integrated management structure with oversight ultimately by the EirGrid plc Board.

3.19 From the information provided by SONI we conclude that neither the SONI Board, nor the SONI MD, has full and transparent oversight of the

management and discharge of SONI TSO licence functions and the allocation of resources available to SONI TSO.

Other elements of the governance framework

3.20 Given that SONI is separately licensed in NI, regulated by UR and funded by NI consumers we would expect that the shared resource model would facilitate a SONI perspective to be developed and articulated which aligns with the needs of NI consumers.

3.21 In a shared resource model we would expect the governance framework to have mechanisms designed to ensure that the interests of NI consumers are protected. However, the information provided by SONI indicates that key protections for NI consumers are either missing or not working as intended:

- There is no Service Level Agreement in place between EirGrid plc and SONI Ltd. such that the SONI Board could approve or monitor prescribed performance levels and value for money from a shared management organisation
- The evidence we have received appears to indicate that there is no SOA in place between EirGrid and SONI TSOs, as required by the Licence, which should set out the interface between the two TSOs and facilitate and enable constructive challenge and resolution of differences between the TSOs. SONI states that it is “confident it fulfils the requirements which a SOA is designed to enable it to fulfil, through the cohesive team structure”.
- The Group Cost Allocation and Recharge Policy provides the basis for cost allocation across the EirGrid group. We have seen no evidence of a performance management or approval process in place to ensure that SONI is provided with appropriate costs and service to allow it to judge whether EirGrid is acting in a manner which protects the interests of NI consumers. The implications of how this policy is operating are considered further in Section 4.
- SONI Ltd. risks are identified and mitigated through the management structure and captured within the integrated framework of EirGrid's top-down/bottom-up approach to risk management. We have no assurance that a holistic picture of risks facing the SONI business is maintained and that these risks are monitored and managed by SONI.
- No SONI specific arrangements to manage conflicts of interest between the two TSOs has been evidenced by SONI. Nor does SONI have its own whistleblowing policy. Any instances of whistleblowing are reported as they arise by the Group Head of Audit and

Does SONI meet the vision for good governance?

3.22 The information provided by SONI indicates that within the EirGrid Group, the model applicable to SONI is highly centralised, characterised by a strong plc Board, a limited Board at subsidiary level, a range of corporate policies applicable to subsidiaries, and pooling of subsidiary resources in a shared resource model reporting upwards to the EirGrid plc Board.

3.23 As a consequence management and oversight of SONI TSO licence responsibilities are effectively discharged by EirGrid plc and not by SONI Ltd. In addition, the integrated governance structures of the EirGrid group do not seem designed to enable SONI to act as an equal partner nor even to be perceived as an equal partner with a mind of its own. In addition there is no robust set of rules to govern collaboration between the TSOs. These, are either missing or not working as set out above. Overall, therefore we consider that SONI's present governance arrangements do not meet the vision for good governance set out above.

4. Issues raised with the regulation and governance of SONI TSO in the CfE responses

4.1 The CfE set out the aims of the governance review together with a list of detailed questions designed to gather information to help UR fulfil these aims. This section sets out a summary of the issues raised in the CfE responses in order to assess whether actual or potential harm exists to electricity consumers in NI as a result of SONI's current governance arrangements. Our assessment draws on the non-confidential responses we have received to the CfE and SONI's subsequent response to UR's information request. Fuller details of the responses can be found in Annex 1. Annex 2 summarises SONI TSO's governance arrangements drawing on SONI's responses to the CfE.

The Evidence of Harm or Potential Harm

4.2 In this section, we consider the extent to which the evidence we have reviewed since the publication of the CfE indicates actual or potential harm to electricity consumers in NI arising from the current SONI TSO governance arrangements. In this context, we have viewed "harm" in the context of our statutory objective to protect the interests of consumers, wherever appropriate by promoting effective competition, whilst having regard to:

- The need to secure that all reasonable demands in NI or Ireland for electricity are met; and
- The need to secure that licence holders are able to finance their activities.

4.3 In respect of SONI TSO, we are required by law to carry out these functions in the manner which we consider best calculated to promote the efficient use of electricity and efficiency and economy on the part of the Licensee; protect the public from dangers; secure a diverse, viable and environmentally sustainable long-term energy supply; etc. We undertake these obligations through the granting and ongoing development of the licensing regime under which SONI operates.

4.4 Consistent with these objectives, responses to the CfE allowed the identification of three potential areas of harm:

- Inappropriately higher prices;
- Network development misaligned with NI policy and user requirements; and
- Barriers to Competition.

4.5 We note that some respondents to the CfE suggested other issues outside these three categories and which are not related to UR's governance review of SONI, e.g. a number of matters related to the SEM. Points from the responses which we consider fall outside the scope of the CfE are noted in Annex 1.

4.6 The three potential areas of harm are discussed further in the following paragraphs.

Inappropriately higher prices

4.7 Harm is caused to NI electricity consumers if electricity prices are higher than they should be. These prices cover all the elements of the industry involved in the production and delivery of electricity, including those of SONI TSO.

4.8 As SONI TSO is a monopoly, its contribution to the energy bills of consumers is constrained to an "allowed revenue" as determined by UR. UR aims to protect consumers from this area of harm by setting the allowed revenue at its determination of the efficient level of costs for SONI TSO.

4.9 In common with utility regulators elsewhere, UR is at an "information disadvantage" compared to the managers of the utilities it regulates. It counters this disadvantage by requiring utilities to provide the information and data it requests, and by challenging this information and data based on expert opinion, observed cost growth, and comparison with other utilities.

4.10 There are a number of elements from the responses to the CfE, and our subsequent analysis that highlight an increase in the challenges faced by UR in assessing the efficient costs of SONI TSO. This, in turn, increases the risk that the SONI TSO allowed revenue is set too high causing NI electricity consumers to pay too much. In summary, this risk arises from the following:

- **Lack of Transparency:** A number of responses expressed concern about a lack of, or diminished, transparency in how the costs reported by SONI TSO relate to the actual costs incurred in delivering the SONI TSO licence. In particular, the growth in cross-business charging between SONI and the rest of the EirGrid Group. Consequently, in order to evaluate these concerns, the UR conducted further analysis of SONI's TSO Regulatory Accounts.

Within the notes and addendum to the Regulatory Accounts are disclosed the related party transactions that exist between SONI TSO and the rest of the EirGrid Group. As provided for within the SONI TSO licence conditions, and not part of accounting standards, an addendum to the Regulatory Accounts separately analyses sales and purchases made by and to SONI TSO from the rest of the Group and analyses them by both the source and nature of the cost. There is

also a note to the addendum that stipulates the basis of allocation which is predominantly 'cost recovery' or 'pass through'.

Table 1: Analysis of SONI Regulatory Accounts

	£'m							
	2018	2017	2016	2015	2014	2013	2012	2011
Operating profit as % of Total Revenue	1.2%	2.7%	5.6%	5.0%	4.5%	6.0%	7.8%	9.8%
Total sales recharges from SONI	51.0	25.0	13.7	7.2	6.6	3.7	1.8	2.7
Total purchase recharges to SONI	68.0	32.1	17.4	9.7	7.7	4.9	2.3	2.0
Net purchase recharges	17.0	7.1	3.7	2.5	1.1	1.2	0.5	-0.7

Analysis of these addenda shows the overall scale of recharges between SONI TSO and EirGrid for both sales and purchases has doubled year on year since 2015, whilst operating margin has diminished. The net position has grown from parity in the early years of the analysis to a net take of services from the group of £17m in 2018. This may reflect the centralisation of services and resource at an EirGrid Group level or a change in cost model within the Group and highlights the importance of a robust cost allocation policy. The growing number and materiality of such re-charges has significantly reduced transparency over whether those costs are genuinely and efficiently incurred in the delivery of the SONI TSO licence.

The allocation of costs to SONI TSO is either made on a "broad brush" basis (e.g. SONI TSO takes 25% of overall costs) or is based on a management assessment. Ideally, this should be more objectively linked to the actual cost of resources deployed to, or needed by, SONI TSO.

- **Limited incentives to challenge costs:** The evidence we have reviewed in response to the CfE suggests the governance structure does not support a culture within SONI TSO where it is routine to

challenge whether costs, projects or policies are appropriate for NI:

- ◆ The governance structure does not allow SONI TSO to challenge or formally agree its allocation of costs;
 - ◆ A significant number of individual responses to our CfE were made on a confidential basis. This may indicate concerns of personal consequences for sharing views with us that differ from the current culture within SONI TSO;
 - ◆ Some responses encouraged UR to review the nature of and the growth in cross-business charging between SONI and the rest of the EirGrid Group, suggesting that this may have led to an increase in the costs of SONI TSO overtime; and
 - ◆ Denial or undermining of mechanisms that would otherwise ensure that any differences between NI and Ireland are considered by SONI and EirGrid TSOs, and any issues are resolved transparently. This is mostly clearly evidenced in SONI's statement that the "System Operator Agreement" between itself and EirGrid TSO has been 'internalised'. UR does not accept that such internalisation fulfils the requirement of the licence obligation or negates the need for there to be such a licence obligation. Where such differences do exist, applying a "one-size-fits-all" approach to the island of Ireland may lead to increased costs for SONI TSO.
- **Sub-optimal procurement decisions:** This is the risk that things are procured that fit the need of the Republic of Ireland system better than they meet the requirements of that for NI specifically. This, in turn, could lead to higher costs to operate SONI TSO than would otherwise be the case, e.g.:
 - ◆ **Gold Plating:** The "things" that are bought include features that are not required for the NI system. Without an active challenge from SONI TSO Management and Board at the time of the relevant purchase, information on the incremental cost of such features may well be lost. This loss of transparency significantly increases the challenges faced by UR in identifying the correct proportion of such costs to be borne by network users in NI.
 - ◆ **Retro-fit:** The "things" being procured may work well with the systems in the Republic of Ireland, but require additional investment to work with the systems in NI. With an active challenge, this may increase the costs allocated to SONI TSO

(and, prima facie, the NI consumer), as the pro-rata share of the overall investment plus the full cost of any NI specific work may be higher than buying “things” that worked with the Northern Ireland system “out of the box”.

For example, a need for a retrofit may occur for any systems that rely on Smart Metering (for example to reduce the need for network investment through active management of the combined Transmission and Distribution System). The level of smart metering deployment, and the underlying protocols for the management of Smart Meters, differ between Republic of Ireland and NI⁹ which means a system that works in Republic of Ireland may need additional investment to work in NI.

Misalignment in network development

4.11 NI electricity consumers would be harmed if the state of SONI TSO’s management of the NI network means its network diverges from NI users’ and policymakers’ requirements to the extent that:

- **Reliability drops:** leading to increased disruption to the electricity supplies of consumers in NI;
- **Connection issues arise:** leading to increasing costs and/or time needed to connect new generation or demand within NI.

4.12 The evidence we have reviewed from the responses to the CfE suggests a number of factors that could increase the risk that harm could arise in this area, notably:

- **Denial of differences between NI and Republic of Ireland:** (see above (p.32))
- **Unconscious bias:** The lack of a clearly defined role for SONI in the sign-off of, or challenge to, costs or plans leading to an unconscious bias in the prioritisation and approval of projects, with those needed for the needs of NI consumers being seen as lower priority.

Barriers to Competition

4.13 UR’s statutory duties require it to promote competition where it is an effective and appropriate measure to protect the wider interests of consumers. For

⁹ This difference in smart metering protocols is acknowledged in the EU Clean Energy Package, which seeks to address the issue by harmonising these protocols across the EU. This harmonisation will take time to achieve, and may not apply to the UK post Brexit – so differences in this area will continue.

this area, only limited evidence of potential harm was submitted in response to our CfE.

4.14 SONI TSO has a role in facilitating competition albeit, as a monopoly provider, it does not face competition itself. This role in the facilitation of competition has a number of elements:

- **Economic dispatch:** As System Operator SONI is responsible for the dispatch of generation; that is, deciding which generation plant should produce electricity at any specific time. In carrying out this role, SONI TSO is facilitating efficient competition between generation plant towards delivering reliable and low-cost electricity supplies. Our review of responses to the CfE does not indicate any harm in this area.

The Generation Market for the island of Ireland is operated as one – meaning the scheduling and dispatch is operated by EirGrid and SONI TSOs to deliver the least cost generation mix for the island as a whole. This co-optimisation of the Republic of Ireland and NI systems is a direct result of considered legislation in the Republic of Ireland and NI. Evidence presented to us does not suggest this as an area of harm in its own right.

The activities of SONI TSO (and EirGrid¹⁰) in this area are subject to a periodic audit to provide comfort and assurance that dispatch decisions are objective and consistent with optimising system costs. This audit would highlight any Scheduling and Dispatch actions that were inconsistent with competition (provided the auditors were aware of those actions).

- **System Service Procurement:** The stable operation of an electrical power system requires a number of services that are deployed alongside the scheduling and dispatch of generation. For example, these services can relate to the ability of generation plant to change its output at very short notice, or to provide reactive power. These services are procured directly by SONI and EirGrid TSOs to meet the requirements of the NI and Republic of Ireland systems.

The effectiveness of competition to provide these services in protecting the interests of NI electricity consumers depends on there being no unreasonable barriers to participation in that competition. Such barriers could arise, for example:

¹⁰ https://www.sem-o.com/documents/general-publications/Scheduling_Dispatch_Process_Audit_ToR.pdf

- ◆ From a bias to buy services provided in specific geographical areas, where that bias is not justified in terms of the underlying physics of the power system; or
- ◆ By configuring the competition in a way that places some potential suppliers at an unreasonable disadvantage – for example based on where their company is registered, or their offices are based.

The evidence suggests that a number of factors may increase the risk of barriers to competition arising in each of these areas.

- ◆ **Centralised, group-wide, procurement:** Centralised purchasing of services by EirGrid Group is covered by EU Procurement legislation, with requirements published in the Official Journal of the European Union, and demonstrably objective selection of winners.
- ◆ **Denial of differences in the systems of NI and Ireland:** This could lead to requirements and contracts for System Services being drafted in a way that limits the effective participation of service providers in NI.
- **System analysis:** The development of policy and regulation for the electricity industry is informed by analysis of how policies or regulations would impact the underlying system. This analysis is often carried out by the relevant TSO.

It is essential that policy makers and regulators are able to rely on the analysis of System Operators, with a clear understanding that the objectiveness of this analysis has not been compromised. In this context, an institutional denial of differences between the NI and Republic of Ireland systems indicates a risk that SONI and EirGrid's joint analysis may not fully recognise areas where the impact on the system in NI differs from that in Republic of Ireland.

SONI TSO Governance: potential for conflict between aims of shareholders and consumers

4.15 This section draws on responses to the CfE and highlights features of SONI TSO's governance which increase or potentially increase conflict between the aims of shareholders and consumers within NI in forming trust and confidence in the relationship. We have grouped the points arising from these submissions under the following headings:

- Scope of Decision Making
- Cost and Benefit Allocation; and
- Prioritisation of the Republic of Ireland's economy.

Scope of Decision Making

4.16 In considering this issue, we have reviewed further information provided by SONI covering the specific arrangements for its governance. Having considered this additional information alongside other responses to our CfE, we now consider that the observations on the scope of decision making are made up of a number of specific issues. Notably:

- Restrictions on the SONI Board;
- Empowerment of SONI TSO Management; and
- Procurement led from EirGrid's Head Offices .

Restrictions on the SONI Board

4.17 At the time of writing, whilst there is a SONI Board, its ability to influence and challenge decisions impacting NI electricity consumers is limited. This limitation flows, in turn, from a number of factors:

- **Reserved Matters:** The matters that are reserved for the SONI board are limited and do not give it the right to challenge or agree plans for System Operation in NI or to challenge the costs or level of service arising from transactions with the EirGrid Group
- **Lack of System Operator Agreement:** (see 3.21 above).
- **Board Membership:** The evidence in this area suggests limited independence from EirGrid plc. Specifically:
 - ◆ There are no independent members on the SONI Board;
 - ◆ At the time of writing, all SONI Board Members are either members of the EirGrid Executive team or members of the EirGrid Board (including the acting SONI MD); and
 - ◆ The Managing Director of SONI has historically had no dedicated direct reports; instead there are a number of staff that report through a “dotted line” relationship, with their main (solid line) relationship being with a manager in EirGrid plc. We are aware of recent proposals to change this and introduce

direct reports in a few key areas.

This lack of independence in Board Membership limits the extent to which UR can assume an alignment between its statutory objectives to protect the interests of NI consumers and those of the SONI Board.

- **Common Resource Pool:** EirGrid operates a common resource pool across the whole EirGrid Group, which includes EirGrid and SONI TSOs. Whilst this can be argued to support efficiency, it gives rise to two issues that potentially contribute to harm to the NI electricity consumer:
 - **Reduced cost transparency:** The mapping of the costs that arise from each member of the resource pool to SONI TSO is not transparent and, as noted in Paragraph 4.8 above, the level of the costs charged from EirGrid has risen in recent years.
 - **Reduced ability to challenge:** Limiting those staff dedicated to SONI TSO diminishes its ability to challenge (both in terms of appropriateness and cost) the overall plans for, and approach to, System Operations in NI.

In practice, the SONI Board cannot be entirely effective in ensuring that any NI specific issues are addressed without objective analysis and advice from staff that report to that board.

Empowerment of SONI TSO Management

4.18 As noted previously, there are limitations on the extent to which SONI TSO managers are able to challenge policies, projects and budgets to ensure that they are appropriate to the needs of NI consumers, in particular arising from:

- Use of a common resource pool which means that significant dedicated SONI TSO managers and staff do not really exist;
- Centralisation of roles and functions in EirGrid's Head Offices, such as procurement and regulation; and
- The internalisation of the System Operator Agreement, suggesting a corporate view that legitimate differences between the transmission systems and operations of NI and Ireland are small or non-existent.

4.19 With SONI TSO management and staff reporting into EirGrid plc and with a centralisation of more senior roles to EirGrid's Head Offices, there is a significant risk of the formation of a culture that suppresses any challenge to policies, projects and budgets for NI specific reasons.

Procurement led from EirGrid's Head Offices

4.20 While common procurement can reduce costs and benefit consumers in NI, some respondents have noted that costs have gone up since procurement was centralised in EirGrid's Head Offices. This could happen, for example, if items acquired for the all-island system may be over-specified for NI or may require adaptation to be used in NI: in each case, the additional costs imposed on NI consumers may exceed the benefits of common procurement.

Cost and Benefit Allocation

4.21 A number of respondents to our CfE noted concerns that the allocation of costs between SONI and EirGrid TSOs may not be equitable, meaning that NI electricity consumers face a higher proportion of costs than would otherwise be the case.

4.22 The issues relating to allocation between SONI and EirGrid TSOs have been discussed earlier in this section, with the main issue relating to the sharing of costs and the lack of transparency in inter-group transactions, and approval by an effective SONI Board.

Prioritisation of the Republic of Ireland's economy

4.23 A number of respondents to the CfE questioned whether the fact that SONI is now ultimately owned by the Government of Ireland means that SONI's and/or EirGrid's decisions will act to favour the economy in the Republic of Ireland over that of NI. Specific items noted in these responses include:

- That the existence of NewEra¹¹ (a Government of Ireland body with oversight of the commercial state-owned companies) indicates a desire to ensure that these companies (including EirGrid) work to the benefit of the Republic of Ireland as a whole. The relevant submission (in response to the Call for Evidence) goes further, and suggest this acts to undermine NI;
- A perceived prioritisation of doing the things necessary to connect new demand (e.g. data centres) around Dublin, and suggesting this focus undermines the interest of NI consumers; and
- Delays to the North/South interconnector that would strengthen electrical links between NI and the Republic of Ireland. This in turn would reduce the cost of electricity to NI consumers – albeit also reducing the need for power stations that are local to NI.

¹¹ New Economy and Recovery Authority

4.24 UR notes the above concerns, but is not persuaded that there is evidence available in support of them or which establishes harm or potential harm that arises from the ultimate ownership of SONI by the Government of Ireland. In particular, we note that:

- Connecting new business in and around Dublin does not harm NI electricity consumers unless these new connections have been achieved by degrading the NI system. From the evidence available to UR, this is not the case; and
- Delays to the North/South Interconnector do harm NI electricity consumers; however, the barriers to this interconnector's progress are outside the control of either SONI or EirGrid TSOs. The delays arise from difficulties in obtaining planning consent to build the new wires. These delays are non-partisan, with barriers to the project from planning authorities in both NI and the Republic of Ireland. We have no evidence to suggest that delays in obtaining planning approval have been caused by negligence on the part of SONI or EirGrid.

5. Remedies available through existing regulatory framework

5.1 In this Section 5, we consider the existing provisions for the regulation of SONI, as set out in its licence and the extent to which these can address the issues observed in the governance of SONI TSO. These reflect concerns in two areas:

- The risk of harm to consumers discussed in Section 4 above (inappropriately higher prices, misalignment of NI policy and SONI approach to network development and barriers to competition); and
- That necessity for UR (and the Department of the Economy) and wider stakeholders to have full trust and confidence in SONI TSO as a responsive and willing provider of transparent and objective analysis and NI-focussed advice in order to aid the transition to a Low Carbon Economy and implement the NI Executive's energy strategy

5.2 In general, the existing regulation is based on a dialectical paradigm, with (in simple terms) SONI representing the interest of its shareholders, and UR representing the interest of consumers. The nature of this current relationship is inconsistent with developing the trust required to effectively manage NI's transition to a Low Carbon Economy in the UK context.

Measures in the current SONI TSO licence

5.3 The TSO licence places a number of obligations on SONI and its TSO Business. Given the perceived harm or risk of harm which has been distilled from the CfE, we have considered the existing content of the TSO Licence relevant in mitigating those concerns with a view to understanding the extent to which:

- The existing drafting and operation of the Licence provides adequate protection in order to alleviate the concern;
- The existing drafting adequately addresses the concern but the implementation could be strengthened to better manage the risk; and
- There is a residual risk that is not adequately addressed in the current license drafting.

5.4 This section highlights mitigating controls in relation to each of the areas where Section 4 identifies a risk of harm.

Prices

5.5 Fundamentally the scale of prices charged to users of the network are

restricted under Condition 32 of the SONI TSO Licence (Price Control). Additionally, System Support Services are procured and reported in line with Condition 29, in line with a published statement approved by UR while Dispatch Balancing Costs are reported annually under Condition 39 in a form approved by UR. However, given the lack of robust comparators, future price controls and incentives will be based upon the historic information provided annually within the Regulatory Accounts and Reporting of Costs and Outputs spreadsheet and as part of explicit price control submissions. Hence, in part, future prices will be determined by costs reported by SONI TSO:

- **Increased scale of recharge:** Condition 2 requires SONI TSO to prepare audited accounts including disclosure of related party transactions. Whilst the accounts are audited and approved by the SONI Board, the transactions themselves are not specified within any Service Level Agreement (SLA) or approved by SONI directors. Paragraph 2(b) of Condition 24 “System Operator Agreement” (SOA) requires that the SOA provides for the sharing of costs and making of payments but as there is no SOA in place this obligation is not being met. SONI has stated in its responses that it is confident it fulfils the licence obligation through the cohesive team structure it maintains. UR does not accept (and has not previously accepted) that such internalisation fulfils the requirement of the licence obligation or indeed negates the need for the licence obligation and therefore for an SOA to be in place.
- **Allocation of costs:** Condition 2 requires that UR must approve any change in accounting policy or apportionment. The nature of the related party transactions should be disclosed under that same condition within the Regulatory Accounts and supplementary Reporting of Costs and Outputs spreadsheet. EirGrid’s policy on apportionment is regularly reviewed and a copy provided to UR. That said, the basis of apportionment within that statement remains high level and the resulting costs are not approved by the SONI Board, although they are approved in aggregate in the signing of the audited Regulatory Accounts.
- **Challenge of costs;** Condition 24 requires there to be a SOA between the two licensees but as highlighted above this obligation is not being met as there is no SOA currently in place. The provisions within the Licence require the SOA and changes to it to be approved by UR and the document published to ensure transparency and challenge amongst stakeholders. It is clear from comments received to the CfE that there is no SOA in place and therefore there may be potential breach of Condition 24. SONI has also confirmed that the SONI Board does not have a formal role in procurement decisions

other than its overriding duty to act in the interest of its shareholders and other stakeholders. At present there is no Licence obligation to implement a Service Level Agreement reflecting costs and service levels by which the Board can oversee and approve costs received from EirGrid and therefore only a general Group Cost Allocation and Recharge Policy developed jointly between SONI and EirGrid plc.

- **Cost differentials between the two TSOs:** as discussed above, the allocation of costs is specified within the EirGrid policy but this is high level and does not generally specify individual cost drivers. That said, Condition 2 requires UR approval of any change to accounting policy or cost apportionment. Additionally, Condition 41 “Regulatory Instructions and Guidance” provides for the UR to stipulate how it wants cost and network data to be submitted in order to effectively regulate the TSO and set price controls.

5.6 UR therefore has sufficient powers under the Licence to understand and specify the nature and disclosure of costs and network data for the purpose of setting price controls. However, in the absence of a SOA and an SLA, the absence of dedicated management resource for the SONI Board, and the lack of effective Board sign-off of those individual transactions, we believe there is little SONI ownership and accountability of those costs.

Network development

5.7 The functioning and security of the state of the NI network is ensured through the stipulations of several Licence Conditions, for example:

- **Reliability:** reliability and security standards are managed through explicit Licence Conditions which are overseen by UR either through SONI TSO annual reporting and/or robust change mechanisms. Failure to operate within these requirements would be a breach of Licence exposing SONI to enforcement or financial penalty;
- **Connection:** Under Conditions 25 and 26, SONI TSO is required to offer terms to connect to and use the network on a non-discriminatory basis (between persons and groups of persons). There is also transparency in terms of the potential for connection through conditions 33, 34, 35 and 40 which require SONI TSO to publish details of capacity and investment plans to provide transparency for users and would-be users;
- **Differing network characteristics:** Condition 41 “Regulatory Instructions and Guidance” (RIGs) allows UR to stipulate the detailed nature by which SONI TSO should collect and report network data to allow UR to regulate the TSO effectively and conduct and monitor a

price control. Moreover, Conditions 33, 34, 35 and 40 bring greater transparency to both UR and users in respect of the state and capacity of the network;

- **Resources:** as above, in considering the operation of the network in NI in comparison to users' expectations and that of the Republic of Ireland network, the Licence gives sufficient ability for UR to understand the state of the NI network and to monitor it over time. Condition 3 also ensures that SONI is provided with sufficient management resources and financial resource or facilities to enable it to carry out the TSO business and requires EirGrid to provide annual audited certificates of providing sufficient financial resources to meet SONI TSO Licence conditions. Condition 3A also provides for a parent company undertaking requiring SONI to procure from EirGrid plc a legally enforceable undertaking to the effect that EirGrid plc shall ensure that at all times (i) SONI TSO shall have adequate financial and non-financial resources in order that it may perform its obligations and discharge any liabilities arising under the SONI TSO Licence and (ii) it guarantees in full as and when they fall due the performance of such obligations and the discharge of such liabilities.

The SONI TSO Licence under Condition 12 "Independence of the TSO Business" does not stipulate that **the two TSO Licensees** of SONI and EirGrid are required to be independently managed or resourced and explicitly states that it does not apply to any holding company when specifying the need for independence of the SONI TSO from any affiliates not involved in the business of the TSO. The Licence does require the publication, and annual review, of an approved compliance plan and the appointment of a Compliance Officer to report annually on the operation against that compliance plan. We understand that no compliance plan currently exists. There are also additional Licence Conditions¹² which prohibit cross subsidy and discrimination and include the appointment of a Compliance and Assurance Officer¹³ to verify the Licensee's compliance with these conditions. As discussed previously, the Licence¹⁴ also incorporates the need to maintain a System Operator Agreement to define and manage the interactions between the two businesses, but on the evidence submitted there appears to be no such agreement currently in place. Both the Compliance Plan and SOA, required to be published as part of the Licence Conditions, do not appear to be

¹² Condition 5 "Prohibition of Cross-subsidies";
Condition 11 "Restrictions on the use of certain information"; and
Condition 15 "Non-discrimination"

¹³ Condition 23B "Compliance and Assurance Officer"

¹⁴ Condition 24 "System Operator Agreement"

maintained and hence there is a lack of transparency to users around the formal interaction between the two Licensee businesses in areas such as outage planning, system planning etc., and also the operation of any affiliate.

5.8 UR therefore has sufficient powers under the Licence to both set out and monitor the state of the network within NI. Whilst SONI state that the principles of Condition 24 (SOA) are being complied with, we have never accepted this as effective assurance and we will engage separately with them on the lack of a SOA as required by Licence. At the outset of this consultation, we were of the opinion that Condition 12 was not wholly clear in its scope, intent and implementation. This lack of clarity has also been raised by a number of respondents to the CfE. As part of a separate discussion with SONI as appropriate, we will consider the current drafting of Licence Condition 12 in order to improve its clarity of purpose. We will also raise with SONI the lack of a current approved Condition 12 business separation plan to further improve transparency although no valid concerns were raised in its implementation as currently worded.

Competition

5.9 As discussed previously, the Licence is predominantly concerned with ensuring that the interests of NI consumers are protected, including by promoting competition in generation and supply. This is achieved by the Licence being transparent in setting the levels of service and security that consumers enjoy, whilst capping prices via an effective price control. It also binds the Licensee to comply with a number of market mechanisms as well as incorporating a number of behavioural requirements:

- **Economic dispatch and procurement of System Services:**
Conditions in the Licence require the TSO to schedule and dispatch units in line with forecast demand and security and planning standards and produce an annual audited report on its activities. The Licence also requires the TSO to operate the Balancing Market to a merit order and for the TSO to produce and maintain a Balancing Market Principles Statement and separately a System Support Services Procurement Statement as well as maintaining a Capacity Market Code.

In addition, and as already discussed, the Licence also prohibits the TSO from giving a cross-subsidy or from sharing information that should remain confidential to its business, as well as prohibiting discrimination between any person or class of person. Licence Condition 23B requires the TSO to appoint an independent member of the management team to oversee and report on compliance with these requirements; and

- **System analysis:** As already highlighted, the transparency with which SONI TSO acts to plan, maintain and operate the network is provided through a number of Licence Conditions. The minimum standards to which the network is managed are also prescribed and agreed as are the costs and investment necessary to achieve those over a price control. There is also sufficient feedback provided within those documents to raise any concerns with either The Compliance Officer or UR directly should a party feel unfairly discriminated against.

5.10 The Licence as drafted has sufficient obligations which govern the behaviours of SONI in meeting its statutory objectives to protect the interests of consumers by promoting effective competition in generation and supply. As highlighted in Paragraph 5.8 we will discuss with SONI redrafting of Condition 12 to improve its clarity of purpose as well as obtaining publication of a current Compliance Plan by SONI to improve transparency amongst stakeholders.

Initial Conclusions

5.11 Some of the areas of concern raised by the responses to the CfE are either outside of the scope and vires of UR, or are adequately addressed within the current TSO Licence. In addition there are also two specific areas of the Licence that concerned respondents on which we will engage separately with SONI, namely the lack of a SOA, and the current understanding of Condition 12 and publication of the associated current business separation Compliance Plan.

5.12 Our analysis does however identify several areas of concern raised and not sufficiently mitigated within the Licence:

- **Management and Decision Making in a shared management and resource model:** we believe that a shared management and resource model maintains the risk that decision making across all aspects of the business could be made potentially to the detriment of NI consumers. Such decision making could reflect EirGrid plc priorities and seek to implement them through the shared management hierarchy, overriding the priorities and specific drivers of NI consumers and users, Effectively a one-size fits all approach which maximises parent company value. We believe such concerns are not sufficiently mitigated by the existing Licence and governance structure which principally focuses on both consumers within NI and Republic of Ireland, or by the restructure recently proposed by SONI and EirGrid to increase the dedicated resource within SONI in the areas of Regulation, Strategy, and Stakeholder Engagement;
- **Objectives of management and staff aligned with those of the shareholder:** we believe that under a shared management and

resource model, where ultimately the majority of staff report through an EirGrid Executive Director to the EirGrid CEO, the objectives of staff align with those of the shareholder, in terms of priorities, progression and reward. Without a sufficiently strong SONI Board to set and drive the delivery of SONI TSO specific business priorities, we are concerned about the lack of protection for NI consumers; and

- **Plans, policies, cost and benefit allocations are not approved by an effective SONI Board:** without an effective SONI Board we are concerned that NI consumers will not be adequately protected. Policies adopted on a group wide basis and a shared management model raise the concern that plans are adopted on a 'one-size fits all' basis with a shared investment committee structure. Cost and benefit allocations are attributed and aligned with a corporate allocation policy using high level cost drivers determined by shared management.

5.13 We are therefore concerned that the above areas could potentially give rise to:

- **Inappropriately higher prices for NI consumers**, particularly through the obfuscation of information including the increasing levels of inter-company recharges disclosed within the Regulatory Accounts of SONI TSO. The price control process to set prices is predominantly based upon historic cost trends, there being a lack of a robust and efficient comparator for SONI TSO, and hence there is a concern over the shareholder incentive to make cost information transparent to the regulator compounded by the lack of an effective SONI Board and associated SLA to agree and approve those costs;
- **Misalignment of NI policy and SONI approach to network development** through a 'one-size fits all' approach to investment and operational decision making in a shared management model and decisions therefore risk being taken for the benefit of all users and consumers and not NI consumers specifically. This also includes the risk that NI network and user differences are not sufficiently encapsulated within decision making; and
- **Barriers to competition** whereby, again, the shared management and operating model employed across EirGrid and SONI TSOs risks a 'one-size fits all approach' and potentially denies differences in developing and operating the NI network, including in system analysis and planning.

5.14 It should be noted that these concerns do not arise from the fact that EirGrid is owned by the Government of Ireland. Whilst a number of respondents

expressed a range of concerns with the ownership of SONI, there was no explicit harm identified and the concerns expressed were either outside of the statutory responsibilities of SONI and the regulatory framework, or mitigated by the obligations being complied with in the TSO Licence. Many of the concerns expressed by stakeholders resulted from the fact that the two Licensees were operated under a shared management and resource model which would not exist if the ownership of the two Licences was sufficiently separate. As discussed earlier (Paragraph 5.11), this issue is further compounded by the lack of transparency in the two key areas of Licence compliance not currently being complied with and subject to separate dialogue.

5.15 As highlighted in Section 2, a better balance of incentives, between those of the shareholder and consumer, and the need for greater trust and transparency to successfully deliver a Low Carbon Economy has been the subject of much discussion and change in the regulatory environment. This is not just within electricity and NI, but within regulatory frameworks in other utilities and across other jurisdictions. In looking to better develop trust and transparency and establish an appropriate balance of incentives across the different stakeholders, regulators have implemented a number of licence changes with the intention of:

- **Obtaining greater levels of information detail** and more prescription of outcomes to be achieved by regulated utilities. UR currently employs licence obligations as implemented elsewhere and therefore meet best practice. However, whilst more intrusive regulation may gain greater transparency it also risks more delegation of responsibility to regulators and less trust and accountability within regulated businesses;
- **Increasing effective competition** and separating activities across the value chain where this is achievable. To ensure effective competition, business separation rules and reporting are introduced to avoid market distortion from shared ownership. Only where the market can be liberalised and the benefits exceed synergies are these typically progressed; and
- **Greater independence of Board and management** with the potential for balanced objectives between stakeholders better reflecting the needs of NI consumers and users as well as improved trust and accountability. The level and scale of independence of resources to support an effective board needs to be considered against the potential for increased costs and the lack of synergies.

5.16 Chapter 6 looks to address the potential areas of concerns and considers the most effective approach to mitigating those risks given the approaches taken by regulators elsewhere.

6. Remedies Based on Changes to SONI TSO Governance

6.1 In this Section 6, we consider the nature of remedies required to address the issues observed with regard to the governance of SONI TSO. These reflect concerns in two areas:

- The risk of harm to consumers discussed in Section 5 above (inappropriately higher prices; misalignment of NI policy and SONI approach to network development; and barriers to competition); and
- The advent and subsequent implementation of a new NI Executive energy strategy, coupled with other actions to transition to a Low Carbon Economy, necessitating ever greater levels of trust in SONI TSO as a responsive and willing provider of transparent and objective analysis and advice focused on the needs of NI.

6.2 In the Call for Evidence (CfE) we set out a number of suggested options, highlighting the fact that these were not proposals for action, nor necessarily solutions to all the issues that might be raised. They were included in the consultation as a basis for discussion of the kind of policies that could be deployed to mitigate perceived risks and follow best practice seen elsewhere:

- CfE Option 1 – **No change** – leaving SONI free to make its own governance changes within the provisions of the Licence;
- CfE Option 2 – **Clarify Licence Condition 12** – improving the clarity of Licence Condition 12 which sets out the requirements for independence, but with no substantial change proposed to the level of required independence from associated businesses;
- CfE Option 3 – **Managerial independence of SONI TSO** – adding managerial independence of SONI TSO from EirGrid to the SONI TSO Licence and implemented through a revised compliance plan. The SONI MD would be required to be a Board member of SONI and the matters reserved clarified and extended to include a system of effective internal controls to be established to enable risks specific to SONI TSO to be assessed and managed;
- CfE Option 4 - **Option 3 plus strengthening the SONI Board** – changing the Licence to require independence of the SONI Board from EirGrid with the appointment of one or two independent NEDs, including one as chair; and
- CfE Option 5 – **Majority Independent NEDs** – to require the SONI

Board to comprise of a majority of independent NEDs, one of whom would chair the Board. It could be argued that this approach would not preclude SONI TSO from adopting EirGrid strategy, except where in conflict with SONI TSO specific objectives.

6.3 The CfE highlighted a shared view between UR and SONI that Condition 12 is not fit for purpose in its current form and needed to be clarified as to its purpose and means of implementation. This view has been reinforced by the responses to the CfE and confirms that CfE Option 1 is not the right approach to adopt. As a minimum, CfE Option 2 is necessary, not least to clarify the current purpose of Condition 12 but simply amending this Condition does not, (nor is it capable of addressing the two major concerns identified at Paragraph 6.1. Therefore, further changes may also be appropriate to the Licence arising from the outcome of this consultation.

6.4 As to the level of independence required in both management and Board (CfE Options 3, 4 and 5) all respondents who expressed a view believed that further independence of SONI TSO from EirGrid was essential to build confidence that SONI TSO was acting in the best interests of NI stakeholders. There was however no preference as to which of the options was most appropriate with some suggesting CfE Option 5 was safest, others suggesting CfE Option 4 was preferable introducing greater local knowledge and standing, with others comfortable with either of the three options in order to drive change. Some of the respondents cautioned against significantly greater independence of management and resource, concerned that the wider capacity and resource provided by the current shared model may be constrained.

Proposed changes to governance

6.5 Since the CfE we have further considered how to address the governance of SONI TSO consistent with:

- The interests of NI electricity consumers; and
- Best managing the transition to a Low Carbon Economy.

6.6 This consideration builds on the response to the CfE as well as interactions with SONI and other stakeholders. The measures assessed fall into three categories:

- **Independence of the SONI Board**, including its composition and scope ("Matters Reserved" and the need for sub-committees);
- **SONI TSO Management Independence**, being the extent to which the management within SONI are dedicated and report directly to the

SONI Board rather than being drawn from a common pool of “Group¹⁵” resources that are ultimately managed elsewhere; and

- **Other Governance Changes** that we propose in order to strengthen protections for NI consumers. These are: a new licence obligation strengthening the interests for NI consumers; a SONI dedicated whistleblowing policy; greater transparency through the imposition of an effective SLA and SOA; Compliance assurance; Procurement; and the need for a review of the effectiveness of these proposals

6.7 This assessment has led to the development of four distinct consultation options as illustrated in Table 1. Each of these options reflect the spectrum of responses to the CfE and which take forward elements of CfE Options 3, 4 and 5:

- (Option A) a board which draws from the Non-Executive Directors of EirGrid plc considered by EirGrid to have ‘NI background and standing’ but which is supported by a small independent tier of dedicated managers specified within the Licence who oversee delivery of SONI licence obligations via the shared resource model with EirGrid;
- (Option B) an independent board for SONI which is supported by a small independent tier of dedicated managers specified within the Licence who oversee delivery of SONI licence obligations via the shared resource model with EirGrid;
- (Option C) an independent board for SONI which is supported by a dedicated independent SONI management and staff team¹⁶ who deliver SONI licence obligations independently of EirGrid’s shared resource model. With the approval of UR some of these staff or services may be contracted from EirGrid and managed similar to third-party contracts – with defined contracts, SLAs etc.; and
- (Option D) an independent board for SONI which is supported by a dedicated independent SONI management and staff team who deliver SONI licence obligations wholly independently of EirGrid’s shared resource model.

6.8 Each option is supported by a number of common elements, including:

- A new licence condition on SONI Board independence and which

¹⁵ “Group” resources would be shared with other companies in the same group as SONI (subject to business separation rules). At the present time, this is the EirGrid Group.

¹⁶ Some of these staff may be contracted from EirGrid at the discretion of the SONI Board, and managed similar to third-party contracts – with defined contracts, SLAs etc.

provides for a duty to protect the interests of NI consumers and a new compliance plan in respect of these matters;

- A dedicated SONI whistleblowing policy;
- Explicit specification of things (matters reserved) that must be agreed by the SONI Board, rather than at the Board of its parent;
- Requirements for a number of dedicated SONI Board committees to consider issues such as the strategy and plans for the development of the NI Transmission System, along with associated policies.

6.9 The following paragraphs provide a more detailed discussion of issues relating to the independence of the SONI Board. This discussion applies to each consultation option with the main differences being:

- The independence of Non-Executive SONI Board Members;
- The extent of the management roles that report directly to the SONI Board – to balance any lack of independence in that Board; and
- Whether the Non-Executive SONI Board Members are appointed by EirGrid plc or not.

6.10 The following discussion separately considers each of the:

- Composition of the SONI Board;
- Matters reserved to the SONI Board; and
- Board Committees.

Summary of Consultation Options

Table 2: Summary of Consultation Options

		Option				
		No Change	A – Board with EirGrid NEDS	B– Independent Board	C – Standalone SONI potential exemption from UR	D – Standalone SONI no exemption
Board	Licence Duty to require Independent Board	x	✓	✓	✓	✓
	Licence Duty in respect of NI Consumers	x	✓	✓	✓	✓
	Licence requirement for compliance officer and plan for new duties	x	✓	✓	✓	✓
	Licence requirements on SONI Board Composition	• None – Entirely at discretion of SONI Parent	• NED to Chair the Board • SONI MD to be appointed by, report to, and be an executive member of the SONI Board • Number of NEDs to exceed number of executives on Board • NEDs must have relevant experience and appropriate standing • In Options A & B we expect there to be a majority of SONI employed Executive Directors on the SONI Board but would not rule out the possibility of EirGrid plc having one representative on the SONI Board • In Options C-D all SONI executive directors appointed from SONI Senior team (SONI employees)			
			• NEDs can be drawn from EirGrid plc Board • EirGrid selects and appoints the SONI Board	• NED independence to be consistent with UKCGC • Selection and appointment of Board members by the independent SONI Board in a process consistent with the UKCGC		
SONI Board Duties & Matters Reserved	• As delegated by EirGrid plc Board	• Expanded list to be specified in license (See 6.38)			• Approve any changes to Delegated Authority	

		Option				
		No Change	A – Board with EirGrid NEDS	B– Independent Board	C – Standalone SONI potential exemption from UR	D – Standalone SONI no exemption
		<ul style="list-style-type: none"> At time of writing, very limited 				
Management & Resources	SONI Dedicated Management & Resources (to include services)	<ul style="list-style-type: none"> Entirely at discretion of the SONI parent At time of writing, unclear extent of such resources, but seem to be de-minimums. 	UR will require a minimum level of resources reporting to the SONI MD, and independent of other Group companies, for each of: <ul style="list-style-type: none"> Financial Planning Regulation Strategy & Stakeholder Management Engineering Assessment Network Development Planning Operations Procurement 	<ul style="list-style-type: none"> To support an Independent SONI Board UR will require a minimum level of resources (covering at least the areas set out in Option A although an independent SONI Board could request more) reporting to the SONI MD, and independent of other Group companies. Independent SONI and Board to identify the required roles, and appoint the individuals 	<ul style="list-style-type: none"> Direct reports to the SONI MD (The Senior Management Team – SMT) to be as if SONI were a standalone company Appointment and remuneration of SMT individuals and staff to be within control of SONI Board. Any other resources required to deliver the SONI Licence appointed by SONI Board or SMT. SONI may apply to UR for a partial and specific exemption to the requirement to have dedicated management and staff resources. UR may approve on a case-by-case basis (based on a robust cost benefit analysis) including specifying conditions necessary for the protection of NI consumers 	<ul style="list-style-type: none"> Direct reports to the SONI MD (The Senior Management Team – SMT) to be as if SONI were a standalone company fully independent of EirGrid. Appointment and remuneration of SMT individuals and staff to be within control of SONI Board. Any other resources required to deliver the SONI Licence appointed by SONI Board or SMT and fully independent of EirGrid.
	Pay and Incentives	<ul style="list-style-type: none"> Controlled by EirGrid Board 	<ul style="list-style-type: none"> Controlled by SONI Board 			

		Option			
		No Change	A – Board with EirGrid NEDS	B– Independent Board	C – Standalone SONI potential exemption from UR
Other	Conflicts with Group policies and approaches	<ul style="list-style-type: none">At discretion of EirGrid plcNo measures disclosed to UR	<ul style="list-style-type: none">Conflict Policy in place for transparent and documented management of such conflictsSONI Board has ultimate decision to approve any SONI specific approaches – be they based on Group approaches or otherwise.		
	Whistle Blowing	<ul style="list-style-type: none">Controlled by EirGrid Board	<ul style="list-style-type: none">SONI Board required to establish and approve whistle blowing procedures		
	SLA	<ul style="list-style-type: none">No SLA in place	<ul style="list-style-type: none">Formal SLA for all services provided by EirGrid to SONI, or vice-versa		
	SOA	<ul style="list-style-type: none">EirGrid state SOA “Internalised”	<ul style="list-style-type: none">Define and operate to a SOA as required in the existing SONI licence.		
	Compliance Officer	<ul style="list-style-type: none">Not required	<ul style="list-style-type: none">Dedicated SONI Compliance officer required to own a Compliance Plan (for UR Approval) and to report to SONI Board on Compliance		

Composition of the SONI Board

6.11 The SONI Board should work together to provide both leadership as well as effective checks and balances that ultimately support the required level of trust in SONI TSO. As proposed under CfE Options 4 and 5, we believe such a board is likely to need both Executive and NED's to be effective. The role of the Executive and NEDs are complementary, but both are equally important:

- The Executive Directors bring intimate knowledge of the SONI TSO Business
- The NEDs bring a broader view to the company's activities. They have two important contributions to the overall performance of SONI:
 - ◆ They review the performance of the board and of the executive; and
 - ◆ They take the lead where potential conflicts of interests arise. This need has been acknowledged going back to the Cadbury Review, in recognition that the specific interests of the executive management may diverge from the wider interests of the company and its stakeholders.

6.12 As set out in the UKCGC, the Board should also understand the views of the company's other key stakeholders as well as assessing the basis on which the company generates and preserves value over the long-term. It should also consider how opportunities and risks to the future success of the company have been considered and addressed, the sustainability of the company's business model and how its governance contributes to the delivery of its strategy.

6.13 For SONI, the "wider view and challenge" of NEDs should include consideration of:

- ◆ The NI electricity consumer¹⁷;
- ◆ System Operations elsewhere in the world; and
- ◆ Differing perspectives on the Low Carbon Transition.

6.14 The key aspects of the constituency of the SONI Board are further considered in each of the following paragraphs along with how this translates into each of the consultation options. It should be noted that a number of changes were made by EirGrid after the publication of our CfE, specifically the creation and

¹⁷ We propose to make this an explicit licence duty – similar to that placed on GB water companies, as discussed further in "Other Governance" below.

subsequent appointment of a MD for SONI in May 2019 and the appointment of two additional NEDs (the two NI members of the main EirGrid Board) to supplement the three members of the SONI Board on 21 July 2020. Subsequently a third member of the EirGrid Board was appointed to the SONI board in November 2020.¹⁸ Thus the current SONI Board is made up of three persons who also sit on the main EirGrid Board, the acting SONI MD, and two further Executive Directors of EirGrid plc (the latter three all report to the EirGrid CEO, but do not sit on the EirGrid plc Board).

6.15 While we welcome the direction of travel by SONI, we have concerns about whether the structure of the Board will promote good governance compared to one structured along the lines envisaged by the UKCGC. The risks identified do not arise from the individuals on the Board. We would also note that the presence of three NEDs from the EirGrid Board on the SONI Board cannot be relied upon without Licence changes to underpin this composition in the future.

Independence of the Chair

6.16 The Chair has a crucial role in the management of a board in a way that develops trust with external stakeholders. Key elements of this role include¹⁹:

- Ensuring that all relevant issues are on the board agenda;
- Monitoring the balance of board membership to ensure sufficient competence and independence to consider the relevant issues; and
- Ensuring that the NEDs are properly briefed and receive information that is tailored to their needs.

6.17 It is widely acknowledged and a requirement of the UKCGC that this role is best performed by a Non-Executive Chair for the following reasons:

- **Concentration of power:** For the Board to be credible in building trust, it is important that the various interests in a board are balanced, with no one group or individual having unfettered ability to make or block decisions. For this to happen, it is widely acknowledged that the Chair should not be held by an Executive Director. Thinking on this need for independence has strengthened over time:
 - ◆ The 1992 Cadbury Committee stated that the Chair should, in principle be separate from that of the Chief Executive to avoid a considerable concentration of power; and
 - ◆ The latest UKCGC goes further requiring an independent Chair

¹⁸ Tom Coughlan was appointed to the SONI Board on 26 November 2020.

¹⁹ This draws on the observations from the Cadbury Committee 1992 (The Financial Aspects of Corporate Governance) as well as later developments to the UK Corporate Governance Code

with a senior independent NED to act as a sounding board for the Chair.

- **Understanding the needs of NEDs:** The effectiveness of the NEDs of a board depends critically on the information they receive, with that information being prepared by the executive. This is best achieved when the Chair:
 - ◆ Understands the information needs of board members who are not intimately involved in running the business on a day-to-day basis; and
 - ◆ Is of sufficient standing (as an individual, and through their role as Chair) to ensure that the necessary information is made available.

6.18 Based on the above, each of the consultation options envisage a NED as chair for the SONI Board. This is consistent with CfE Options 4 and 5 which were supported by the majority of respondents who provided a view.

Balance between Executive and NEDs

6.19 Several respondents believed that it is important that NI stakeholders understand the role of the SONI Board and who establishes SONI TSO's purpose, values and strategy to ensure public confidence is maintained.

6.20 To establish a level of trust in SONI TSO, it is important that no individual or group has unfettered power at its Board. As such, all consultation options envisage that the SONI Board should be made up of a majority of Non-Executive members – with a MD who will report solely to the Board and not to the EirGrid CEO as present. The nature of the Non-Executive members then differs between Option A and the other three consultation options:

- **Option A: SONI Board with EirGrid NEDs:** The SONI NEDs (with one acting as Chair) can also be NEDs of other companies in the EirGrid Group (subject to business separation constraints), or of the Group itself and it is currently envisaged that these roles within SONI could be fulfilled by the NEDs designated under EirGrid's constitution as having "appropriate standing with extensive NI backgrounds". Whilst not fully independent, the board is reinforced by a small independent tier of management prescribed within the Licence and supported by a SONI whistle-blowing and conflict resolution policy; or
- **Option B, C and D: Independent SONI Board:** The SONI NEDs including Chair are required to be independent as defined in the

UKCGC²⁰. Adopting the UKCGC definitively would also currently require four independent NEDs to be recruited to balance the current executive membership of the board.

6.21 It should be noted that whilst the current SONI board does not include any independent NEDs, SONI state that the EirGrid Board is almost entirely constituted of NEDs, including a minimum of two (currently three) with NI backgrounds. In its response to the information request SONI has also informed us that an EirGrid plc board committee on NI and all-island issues has been established.

6.22 We note that, in this area, some of our consultation options differ in comparison to best practice seen elsewhere and balance the level of independence with an ability to allow some measured co-ordination between Ireland and NI:

- Only Options B, C and D are consistent with the revised governance arrangements for National Grid ESO (as currently implemented) – the Electricity System Operator for GB – whereby those NEDs appointed to the ESO Board cannot also sit on the main board;
- Only Options B, C and D would achieve best practice governance as set out in the UKCGC; and
- Only Options B, C and D are consistent with the mandatory governance arrangements for GB water companies implemented by OFWAT, these options require a majority of independent Non-Executive members

Are executive board members required to be dedicated to SONI?

6.23 Several respondents to our CfE noted that most members of the SONI Board were not dedicated to SONI, and reported to the EirGrid plc CEO. The concern raised with these arrangements is that such Board Members may not necessarily fully consider the specific needs of NI network users and policy makers. For example, this could lead to an unconscious bias to accept things that work for the Republic of Ireland system, but not for NI, without challenge.

²⁰ Impairment of independence of Non-Executive Directors is defined within the UKCGC as including but not limited to a director who:

- Is or has been an employee of the company or group within the last five years;
- Has or had a material business relationship with the company in the last 3 years;
- Received or receives additional remuneration from the company apart from a director's fee;
- Has a close family tie with any of the company's advisors, directors or management;
- Has cross directorships or significant links with other directors;
- Represents a significant shareholder; or
- Has served on the board for more than nine years.

6.24 It is not clear that these concerns can be fully addressed through NEDs, as this relates to the need for intimate knowledge of the SONI business, which is the area covered by the Executive Board members. However, conversely, such separation is likely to detract from the level of co-ordination and co-operation experienced across the two operators and require some duplication of roles across the group with slightly raised costs.

6.25 We are keen to ensure the independence of the Board in aggregate such that no one group has undue influence (which is also the focus of the UKCGC). Under Options A and B we therefore would not rule out the possibility of an EirGrid plc representative sitting on the SONI Board as long as the independence of the board as a whole isn't compromised. In Options A and B we expect there to be a majority of NEDs and in addition the Executive Directors should be majority SONI employees. Options C and D (Standalone SONI) would require the Executive directors to be drawn from the SONI senior management team and thus be independent from EirGrid plc. All options also require the SONI MD to report to the SONI board and not the EirGrid CEO.

Who appoints the board?

6.26 Under normal circumstances, board members are appointed by shareholders, with the UKCGC requiring that this be done in a transparent and objective manner through a Nominations Committee.

6.27 The need for these proposed changes in board composition is to build trust that SONI TSO is appropriately considering the needs of users of the NI electricity networks and how these may change with the transition to a Low Carbon Economy. Whilst shareholders almost certainly have a significant interest in the financial success of SONI, it is less clear that they will necessarily have an interest in these other areas. This has been acknowledged in the establishment of utility regulators to provide a measure of balance between the interests of utility companies, and the wider interests of society as a whole.

6.28 Consultation Option A is based on SONI and its Shareholders selecting all of the Directors (Executive and independent Non-Executive) through a transparent and objective process. However, with an independent board, it may not be appropriate for the Shareholder to have this role. In Options B, C and D we consider that Directors should be selected by the independent SONI Board and should be appointed following a process consistent with the UKCGC. Related consultation questions on Board appointments are set out at the end of this section.

6.29 Regardless of who appoints the Directors, part of the criteria should be that Non-Executive appointees should have appropriate standing with extensive understanding of NI. Such a requirement would be included within a new Licence Condition. Once appointed, the NEDs should meet with UR to understand its

perspective for their new role, a process consistent with arrangements for GB Water companies. The Northern Ireland Electricity Networks (NIE Networks) Licence also requires NIE Networks to demonstrate to the satisfaction of UR, prior to any appointment of a board director, that the appointment will not cause the Licensee to enter into any breach of the requirements as to number of NEDs and their experience. Something similar could be implemented for SONI in all options.

Duties of SONI Board and Matters Reserved

6.30 Members of any Board constituted under the UK Companies Act are subject to a number of Fiduciary Duties set out within the Act and discussed in Section 2. These include a duty to promote the success of the company for the benefit of its members as a whole. That obligation includes having regard to the need to foster relationships with its suppliers and customers and the impact the company's operations has on the community and environment. However, the duty does not explicitly reference final consumers of electricity (they are not direct customers of SONI) and is comparatively weak for interests other than financial success. The extent to which these obligations explicitly align with those of consumers (who are typically not EirGrid customers) is acknowledged to be weak for monopoly utility businesses which can be financially successful without giving much consideration to consumer benefits.

6.31 The imbalance in the objectives of monopoly utilities and their boards has long been acknowledged and is, in itself, one of the reasons that utility regulators exist. Over time, it has become apparent that utility companies can act to hinder regulators in carrying out their role especially through:

- The way they interact with their regulator; and
- The way they analyse and present information to their regulator.

6.32 There are a number of ways this imbalance can be addressed in the case of SONI TSO, including:

- Increasingly intrusive regulation with UR building their own shadow management team. This does little to improve trust and accountability within the monopoly utility; and
- Explicit additional duties to better align its objectives with the needs of users of the NI electricity system and consumers, and those of NI policy makers.

6.33 The latter of the above two approaches is:

- More consistent with building a level of trust between SONI TSO, UR and wider stakeholders such that SONI TSO can be trusted to provide

objective and transparent analysis required to navigate towards a Low Carbon Economy; and

- Consistent with the approach taken by other utility regulators facing similar issues. Most notably OFWAT have amended the licences of England and Wales water companies to require Directors to consider the interests of consumers alongside those on shareholders.

6.34 SONI has cited a number of existing ways that they believe lead to the required protections, including:

- That EirGrid's Licence has obligations for both Irish and NI Consumers for which EirGrid is answerable to CRU;
- The SONI TSO Licence has similar consumer obligations to those of the EirGrid licence in respect of SEMO and the SEM;
- At acquisition of SONI, EirGrid changed its internal corporate documents to, recognise SONI and its responsibility to protect the interests of NI consumers, including its Memorandum and Articles of Association as well as introducing the requirements into the EirGrid plc directors' Code of Conduct.
- SONI also believes that the EirGrid plc board appropriately reflects NI consumer interests through a representation of NEDs (currently three) from NI, and the formation of a sub-committee of the EirGrid plc Board focused on NI and all-island issues.

6.35 In respect of the above, we note that most do not fall within the vires of UR which has no scope in respect of the EirGrid Licence or the composition of the EirGrid plc board.

6.36 As part of our consideration of SONI TSO Governance following our CfE, we became aware of significant limits to the powers ('matters reserved') of the existing SONI Board (the body that is answerable to UR) such that, for example, it had no authority over the SONI TSO budgets. As a subsidiary company, some decisions will be taken at a group level independently of the SONI Board. However, as set out in Annex 2, the matters reserved to the SONI Board are limited.

6.37 In light of the above, under each of the Consultation options:

- The SONI TSO Licence would be amended to require SONI TSO to better align its objectives with and explicitly consider the needs and interests of consumers in NI, in all areas, where it is not already required to consider those needs alongside those of Irish consumers. We envisage that this would be similar to an equivalent licence change recently introduced for GB water companies;

- We propose to specify, in the Licence, those matters that need to be reserved to the SONI Board. Without a regulatory requirement for such reservation, the role and responsibilities of the Board could be limited, and therefore significantly reduce its ability to influence the delivery of its TSO Licence in an efficient manner.

6.38 The reserved matters of the SONI Board already include areas such as appointing auditors; agreeing bank mandates, facilities and guarantees in respect of SONI; responsibility for the company seal and power of attorney; as well as approving financial statements and pension arrangements. Those responsibilities apply to the company and therefore to both the SEMO and TSO licensed activities. We are minded to extend those obligations in respect of the TSO activities only and therefore propose that they are included in the TSO Licence. The list of items that we would propose to require to be reserved to the SONI Board is broken into three areas as follows:

- **Responsibility for Licence Obligations:** The SONI Board is responsible (and accountable to UR) for compliance with and the efficient delivery of the obligations under the SONI TSO Licence. This includes:
 - ◆ Approval of all submissions to UR and public statements / documents required by the TSO Licence;
 - ◆ Being accountable for the development and publication of the SONI TSO Strategic Plan and establish the company's purpose and values and satisfy itself that these and its culture are aligned;
 - ◆ Receipt and consideration of reports from the Compliance and Assurance Officer in accordance with SONI TSO Licence obligations;
 - ◆ Approval of any challenge to regulatory or statutory decisions; and
 - ◆ Being accountable for regulatory disputes involving SONI's TSO Licence.
- **Financial Control:** The SONI Board should be fully responsible for establishing SONI TSO budgets and managing costs within those budgets. This includes:
 - ◆ Approval of SONI TSO opex and capex in line with comparable levels of delegated authority elsewhere in the group, including approval of planned spend;

- ◆ Review of opex and capex financial performance on a regular basis throughout any year in line with budget and Service Level Agreement (SLA²¹);
 - ◆ Establishment and management of business (including capital) planning and budgeting consistent with strategy;
 - ◆ Assuring itself that all procurement processes which relate to SONI TSO activities meet the needs of NI consumers; and
 - ◆ Sign off statutory and regulatory accounts.
- **Internal Management and Operational Policies:** The SONI Board will need to establish and maintain that relevant EirGrid policies ensure that SONI's TSO operations match the existing characteristics of the NI power system, as well as the needs of NI consumers. There may well be cases for drafting SONI TSO specific policies in certain distinct areas, as well as SONI specific whistleblowing and conflict resolution policies.

Board Committees

6.39 The UKCGC requires subcommittees of the Board in areas such as risk and assurance, nominations and remuneration. SONI believes these are unnecessary at a subsidiary level and are managed through a Group board and sub-committees.

6.40 Having considered the specific issues raised in response to the CfE, and SONI Governance more widely, UR believe a number of Board committees will be required, including those required by the UKCGC. The first two of these will be applicable in all options, with the last only applying to Options B, C and D. These committees are:

- **Grid Development and Investment:** A committee is required to explicitly consider the specific requirements of the legacy NI networks, as well as any specific requirements arising from the SONI TSO Licence or NI energy policy. Responses to the CfE highlighted that network development and investment decision making is undertaken by group-wide committees and not approved by the SONI Board. It is not clear from SONI's response to the CfE how these structures ensure that NI specific issues and needs are effectively and transparently considered and, if they conflict with EirGrid's needs, how any conflict is resolved. This committee will ensure sufficient attention is applied to these issues in a transparent way (through committee

²¹ See 6.61 below for our proposal for the SLA.

minutes);

- **Audit, Risk and Internal Control:** The areas covered by this committee have a key role in building trust in SONI and demonstrating (through committee minutes and independent audit) the basis for that trust. In the case of SONI, part of the role of this committee should be to monitor compliance with the SONI Licence, as well as ensuring effective management of SONI TSO risks and costs/budgets.
- **Nominations Committee and Remuneration Committee:** These are definitely required under Option B, C and D with an independent SONI Board needing to ensure its own succession planning, and source appropriately qualified executive and non-executive directors.

6.41 These additional roles could form part of the role of the sub-committees typically required through the UKCGC. We note that such Board committees need not be cumbersome or overly resource intensive and would enhance trust and assurance in SONI. The membership of those committees should include the NEDs who have competence relevant to the sector in which the company operates. We note that the current requirements on National Grid Electricity System Operator (NG ESO) require a 'compliance' sub-committee.

Independence of SONI TSO Management

6.42 To generate trust it is important that, in line with the requirements of the UKCGC, all Board members are appropriately supported with resource capable of doing the analysis, and otherwise preparing information, required by Board members (both Executive and Non-Executive) to understand and oversee SONI TSO's Licence obligations.

6.43 Whilst the SONI TSO Licence has obligations comparable to those set out in the UKCGC and explicitly requires the issuance of annual statements of financial capability and Parent Company Undertakings, a number of the concerns raised within the CfE related to the fact that resources, either directly or indirectly, reported to an EirGrid plc Manager or Director and ultimately the EirGrid plc CEO. As a result, there was concern that this would lead to one or both of:

- The views of shareholders being placed above those of NI consumers; or
- The potential for unconscious bias with those roles being increasingly employed directly by EirGrid in their head office.

Need for dedicated SONI TSO Resource

6.44 Experience would suggest that without adequate resource reporting to

the Board, key decisions might be driven through separate Executive Committee meetings with the Board being able to do little beyond “rubber stamping” those decisions. To avoid this, it is important that the Board has sufficient trusted and capable resource to appropriately challenge those decisions, and the basis for them.

6.45 It is proposed that such resource as required by the Board should be independent and capable of sufficiently overseeing the Licence obligations in the interests of NI consumers. This resource should be sufficiently senior and experienced to provide the SONI Board with the necessary support in the delivery of SONI TSO's Licence conditions.

- In Options A and B, we envisage a small independent tier of dedicated managers directed by the SONI Board. This resource will include analysis to support constructive challenge of the EirGrid view, influencing policy decisions and approving plans with sufficient oversight to ensure delivery through an appropriate shared delivery and operating model. The licence will specify the minimum level of resource needed.
- In Options C and D we propose the level of resource supporting the board will be independent as if SONI were a standalone company and will be directed by the SONI board. This level of resources reflects the fact that in these options SONI will be independent of EirGrid's shared delivery resource. The requirement for independence of resources will be specified in the licence. In the case of Option C, and only with the approval of UR, some of these staff or services may be contracted from EirGrid and managed similar to third-party contracts with defined contracts, SLAs etc.

6.46 We note that in a recently proposed restructure, SONI included dedicated resource in the areas of regulation, stakeholder management and strategy who each report to the SONI MD. This, in our opinion, goes some way to mitigating our concerns but excludes the key functions of finance and engineering/operational competence²². These additional roles are (we believe) critical to demonstrate delivery in areas of the Licence promoting the efficient use of electricity and efficiency and economy and protecting the interests of NI users and consumers.

6.47 This resource is also likely to be key in the reintroduction and maintenance of a sufficiently robust SOA that governs engineering interactions and policy, and an SLA that is sufficiently prescriptive of services and costs capable of being monitored and subsequently incurred being approved by an effective board. Since the vast majority of goods and services are bought at a group level, such resource should also have a role in supporting the procurement process to ensure the outcome aligns with the interests of NI consumers. Whilst this may introduce a

²² Engineering in particular is important to build external stakeholder confidence in SONI leadership and collaboration for the energy transition.

tension between SONI and EirGrid TSOs, this tension is likely to be to the benefit of NI consumers and provide reasonable transparency and accountability of the interactions between the two Licensees.

6.48 In our consideration of potential concerns and options to mitigate risks, we are conscious that there is a spectrum of approaches to management models within the utilities industry and wider economy. To aid the reader's understanding of our proposals we set out a case study (based on a model used in a GB electricity network company) of one approach and how this might work in the case of SONI if applied to Options A and B. Whilst there is a wide spectrum of models, we would highlight the fact that the vast majority employ a degree of integration in order to benefit from synergies whilst balancing this with independent management teams to maintain independence of control, approach and best practice in meeting the needs of differing customer and stakeholder groups. In making our assessment of this balance throughout the paper we have not been able to quantify, and nor have we been provided with an assessment of the benefits that have been generated by the shared management and resourcing model employed by EirGrid and SONI TSOs in fulfilling their statutory duties.

Case Study

The support of an effective board would be achieved through, for example, a small but dedicated management team reporting to the SONI MD consisting of:

- *A **Finance/Commercial Manager** whose responsibilities would extend to the agreement and monitoring of an SLA to adequately define the commercial relationships between SONI TSO and other businesses or entities within the group including cost and service levels; to plan, review and report on the financial performance of SONI TSO on a monthly basis to that management team and through to the board; to ensure compliance with internal group financial policies to the extent that they apply to SONI TSO and to fulfil its statutory obligations; and to be responsible for supporting the Board in the signing of statutory and regulatory accounts and other financial returns to UR;*
- *A **Regulation/Stakeholder Manager** to have oversight of all SONI TSO Licence obligations, including the Price Control, and support an effective board in assuring itself that these obligations are being met; and to engage with key stakeholders to ensure the business, its strategy and plans meet their needs as appropriate;*
- *An **Engineering / Operations Manager** to ensure that all operational obligations are being met, including:*
 - ◆ *the provision of necessary statements required by the Licence;*
 - ◆ *internal group operational and planning policies to the extent that they apply to SONI TSO fulfilling its statutory obligations and adequately protecting NI consumers;*
 - ◆ *any network development plans and business plans reflect and adequately protect the needs of NI consumers; and*
 - ◆ *ensuring that the SOA continues to fulfil the Licence requirement in setting out how engineering and operational activities will be co-ordinated and undertaken when carried out by an associated business or entity.*

In this model there may be a requirement for some additional resource to support these key managers. However, it is not envisaged that these key individuals produce policy, deliverables, or reports. Rather, it is for a shared resource model to develop outputs and appropriate means of delivery and dedicated SONI TSO resource should input to and set additional parameters where required to address NI specific issues. The dedicated SONI TSO resource will need to assure themselves that the outputs meet Licence obligations and protect NI consumers and be able to provide that assurance to the SONI Board. Where there is a conflict, it should be for the Board and/or a conflict resolution policy to resolve, supported by an effective whistleblowing policy. Such a model maintains any synergies extracted from a shared resourcing model but provides greater independence and transparency for the Licensee and consumers.

6.49 Our proposed Options A and B draw from this case study in creating a proportionate but more independent SONI TSO management than exists at present. In Options A and B UR will need to specify the scope of that resource to ensure it is sufficient to provide assurance that the outputs from the EirGrid shared resource model delivered for SONI meet licence obligations and protect NI consumers:

- ◆ **Option A: SONI Board with EirGrid NEDs:** In this option the SONI board is allowed to employ relevant EirGrid NEDs and is therefore not fully independent of EirGrid. Whilst we propose to specify additional ‘reserved matters’ of the board, we also believe there is a case for specifying the scope of the additional resource necessary to be dedicated to SONI TSO to assure us of its independence. These resources would need sufficient seniority, experience and knowledge of the SONI TSO Systems and licence to both constructively challenge the EirGrid view, and provide the support required by the SONI Board.
- ◆ **Option B: Independent SONI Board:** In this option the board will be fully independent in line with UKCGC, but SONI licence obligations will be delivered utilising the shared resource model with EirGrid plc. Consequently we also believe there is a case for specifying the scope of the additional resource necessary to be dedicated to SONI TSO to assure us of its independence. If the SONI Board, following an assessment, considers that additional resources are necessary to satisfy itself of the fulfilment of SONI TSO’s Licence obligations, these additional resources may be assessed by UR. Should we agree with their assessment of the resource and costs being substantially different from our first option then we would initially provide for an allowance of such any additional costs within the current price control.

6.50 Option C is a fundamentally different model. In addition to an independent Board, SONI would be standalone and required to have independence of resources from EirGrid plc. It would directly employ its own management and staff team as needed to deliver SONI’s licence obligations. There would be no shared resource model with EirGrid. However, as this option provides an increased level of independence compared to Option B, we propose to include in the licence condition for Option C, an ability for the SONI Board to assess whether exceptions to the general requirement on independence of resources from EirGrid plc are beneficial and propose these exceptions to UR. These would have to be evidenced as being in the interests of NI consumers and approved by UR who may impose conditions.

6.51 In Option C, therefore, SONI may (with UR’s approval) contract with EirGrid plc for services or resources, including specialist staff which SONI is unable

to or does not wish to employ directly. Such services and resources would be directed and managed by SONI. The rate payable and the quality specification for this resource would be agreed by SONI with EirGrid just as it would be if SONI contracted for services or resources from a third party external to the EirGrid group. The approved SLA would be the contractual vehicle to ensure that services and associated costs are monitored and approved, ensuring transparency.

6.52 We consider that independence of resources should be maintained in the majority of activities (e.g. grid development, connections, network planning, regulation, human resources or legal).

6.53 Option D takes Option C to its logical conclusion and requires SONI management and staff to be fully independent of EirGrid with no exceptions. However, our provisional view at this stage is to rule out Option D because, while a viable option, it would be preferable to have the flexibility that Option C provides. Also, if complete separation of SONI management and staff from EirGrid is taken forward it may be necessary to consider further any impact this would or could have on the current single all-island system control centre which is necessary for the SEM.

6.54 Irrespective of which option is selected, SONI will be required to produce a compliance plan which clearly explains how the SONI organisational structure and management and operational practices align with its licence requirements on separation and independence. This will be a public document for approval by UR.

Other Governance Change Proposals

6.55 In addition to the proposed measures set out above for a more independent, well-supported SONI board, we believe further changes are necessary to enhance confidence in, and support for, a more effective and transparent SONI TSO. These further changes would be required for all options being consulted on but are particularly important in Options A and B as these both retain the shared resource model.

Whistleblowing and conflict resolution policies

6.56 EirGrid currently have a whistleblowing policy that extends across the Group. That policy includes an escalation process including reference to the Group Head of Audit and Compliance, Human Resources (HR) Director and CEO, extending to Chair as necessary. The policy also includes reference to external 'Prescribed Persons' including UR and is published on the SONI website. EirGrid also state they have several mechanisms throughout the group that promote ethical behaviour amongst employees and are developing protocols to prescribe conduct where a conflict or potential conflict could arise. Instances of whistleblowing are reported as they arise by the Group Head of Audit and Compliance to the Audit and Risk Committee of the plc Board. Given the concerns raised within the CfE as to the

shared resource model, we are concerned that such a whistleblowing policy as currently applies to SONI TSO is not effective since the reporting of a whistleblowing event is escalated to an EirGrid senior manager or director.

6.57 In accordance with UR's vision for good governance we wish the two TSOs to work together as equals on an arms' length basis in coming to the best solution for both companies and consumers. Where different views arise between the TSOs they can be better managed through more transparent arrangements incorporated into the SOA and SLA (see below). But ultimately, we remain of the view that effective whistleblowing and conflict resolution policies for SONI are also needed to ensure that unresolved conflict can be raised and resolved in a safe and transparent manner.

6.58 We therefore propose that SONI should have its own whistleblowing policy with an escalation process which reflects the increased independence of its governance. Such escalation routes should therefore include the SONI MD, the NEDs, and an independent Compliance Officer (see Paragraph 6.63) who reports to the SONI Board. It should also clearly identify the Prescribed Person route to raising concerns externally and be published on SONI's website instead of the EirGrid policy. This is consistent with the requirements of the UKCGC which defines good governance as including the ability of the workforce to raise any matters of concern.

6.59 As highlighted in our discussion of Board Duties from Paragraph 6.30 above, lack of competition in System Operation means that the financial success of SONI is not necessarily aligned with the interests of those that use the electricity networks in NI or of NI policy makers. Whilst this can, in part, be addressed through changes to board structure, resource and objectives, this tension between those new objectives and financial objectives remains, particularly across the EirGrid group and across consumer groups.

6.60 In consequence, we will also require SONI to set out in a policy how conflicts of interest should be managed:

- Between SONI and EirGrid TSOs; or
- Within processes and policies which are deemed to benefit all consumers on the island of Ireland, or Irish consumers, over those in NI.

Such a policy should include employees and managers within the shared resource model employed by EirGrid, managers and staff employed by and dedicated to SONI TSO, and directors of SONI in a resolution process, each of whom may identify conflicts of interest.

Management of Group Resources

6.61 To improve the transparency over SONI TSO costs, and demonstrate the effective management of SONI TSO by its Board, we will require SONI to establish contractual arrangements for the management of resources from elsewhere in the Group that are used to deliver the SONI TSO Licence obligations. We anticipate this being in the form of comprehensive and fully costed Service Level Agreement (SLA) which will:

- a) Be signed off by the SONI Board;
- b) Be approved by UR;
- c) Include service specifications and rates; and
- d) Be legally binding between SONI and EirGrid plc.

6.62 The System Operator Agreement²³ must also operate to bring transparency to the operational interactions between SONI TSO and the rest of the EirGrid group where activities were undertaken on behalf of the Licensee.

Compliance Plan and Officer

6.63 As is normal practice for regulated utilities, we will require SONI to draft a compliance plan, for UR approval, as to how in practice it proposes to comply with its regulatory obligations, in particular any new obligations implemented following this consultation. SONI will also be required to appoint an individual as a Compliance Officer who should be otherwise independent of the SONI Management, and that of any related companies.

6.64 The Compliance Officer will:

- Report to the SONI Board;
- Assess the ongoing compliance of SONI with its compliance plan and all of its licence obligations; and
- Provide a report, at least annually, to the SONI Board on its assessment of the adherence to and effectiveness of the compliance plan and licence obligations. This report should also be available to UR.

²³ SONI TSO Licence Condition 24: “at all times maintain in force, an agreement (the “System Operator Agreement”) which: (a) insofar as any matter is within the control of the Republic of Ireland System Operator and affects the ability of the Licensee to carry on the Transmission System Operator Business, ensures that such matter is carried out in a manner such that the Licensee is capable, on a continuing basis, of carrying on the Transmission System Operator Business”;

Procurement

6.65 Procurement for the group as a whole is centralised within EirGrid plc. Specifications for tenders and the tender processes are operated from EirGrid headquarters and regulated through EU law²⁴.

6.66 Where SONI continues to obtain services using this shared procurement specialism as part of the EirGrid Group but where the UK is now outside of the EU, the procurement of good/services which will or can be utilised by SONI TSO shall continue to be advertised in the UK and accessible to economic operators in the UK in the same way as EU economic operators. Such tenders and contracts should be assessed and operated on a non-discriminatory basis and we propose to insert such requirements within SONI TSO's licence. Also where SONI TSO is to be the sole or predominant user of goods or services to be provided to it, the procurement is to be undertaken by SONI itself.

Future review of governance effectiveness

6.67 Our provisional view at this stage is to rule out Option A because it does not go far enough and Option D because, while a viable option, it would be preferable to have the flexibility that Option C provides.

6.68 Our provisional preferred options would be Options B and C. Options B and C are likely to represent the most proportionate interventions considering the evidence we have received. These options should promote a healthy discussion such that legitimate differences of opinion are aired in decision making between the two TSOs to the benefit of NI consumers, while also providing effective transparency and accountability by SONI for the delivery of its TSO obligations. They each allow SONI to maintain scope to deliver synergies and related efficiencies which may arise from SONI's position in the EirGrid group with better alignment of the commercial interests of SONI's shareholder with the interests of NI consumers. Crucially both Options B and C will also ensure increased transparency.

6.69 However, further steps could also be taken as illustrated by Option D which requires the complete independence of the SONI management and staff team from EirGrid plc.

6.70 We will keep any new obligations agreed at the outcome of this consultation under constant review and it will be up to SONI to demonstrate its compliance with any new obligations and that it is an effective partner in all-island TSO decision making. Given the importance of ensuring SONI TSO as a trusted advisor in the ongoing transition to a Low Carbon Economy, we believe it appropriate to undertake a formal review of the effectiveness of SONI TSO governance two years after any new measures have been implemented, with the aim that such

²⁴ Directive 2014/25/EU

review is concluded before the next price control. This review could recommend further changes, including the need for greater independence if found necessary.

Cost / benefit of proposals

6.71 We are conscious that the changes to the constituents of the Board and the additional dedicated resource to adequately support it will impose an additional cost on SONI TSO to be remunerated through the Price Control. The estimated costs and benefit for each option are set out below.

Estimated costs

6.72 The estimated costs (in 2019 prices)²⁵ for each option are set out in the tables below, based on an assumed number of NEDs, Managers, and Analysts for illustrative purposes. All the costs set out below are ongoing costs, upfront implementation costs are stated where appropriate. All the options allow for joint procurement, e.g. facilities management or IT hosting, with EirGrid plc.

6.73 The numbers in the tables, particularly for Option D, are caveated by the fact that the evidence for synergies and efficiencies provided by SONI arising from joint arrangements with EirGrid is limited. SONI's response to the Call for Evidence identified a number of areas where it claimed synergies existed but these were not quantified. SONI's response to UR's information request pointed to examples provided in its price control submissions but when these were analysed the benefit or synergy identified has not been quantified in most cases. As we do not have enough information to confidently estimate the effect of dis-economies of scale in Option D we have left this blank as to use the limited information we have could give a misleading picture.

6.74 In regard to one off implementation costs, these are reduced by the fact that SONI has already created a SONI MD office including additional management resource (for regulation, stakeholder management and strategy). Option B and C will each entail a small amount of one-off implementation costs to recruit new independent Board members. Also, in Option C a small amount of upfront implementation costs would also be incurred to recruit additional staff into SONI who may currently be provided by EirGrid plc. However, we consider that recruitment costs are already provided for under existing allowances for HR/Corporate services.

6.75 In regard to salary costs, SONI TSO's 2020-2025 Price control includes costs for staff recharged from EirGrid and for staff employed by SONI. These costs are together considered sufficient to deliver SONI's TSO licence obligations. This section considers whether the options put forward in this paper merit any additional

²⁵ As per UR's Final Determination for the SONI 2020-2025 Price Control and the EirGrid 2019 annual report costs.

allowance for salary costs.

6.76 Options A and B entail a small amount of additional salary costs at management level above the number determined for SONI TSO's 2020-2025 Price Control. These additional staff would oversee delivery of SONI licence obligations rather than through the shared resource model with EirGrid. Options C and D envisage a dedicated SONI management and staff team who deliver SONI licence obligations independently of EirGrid's direct management. In Option C some of these staff or services may be contracted from EirGrid with the approval of UR, but we would expect SONI to employ as many staff locally as possible.

6.77 It may be the case that additional salary costs arise in Option C or D for management and other staff due to synergies or economies of scale with EirGrid being lost. The issue is complicated by the fact that SONI has not provided robust evidence of synergies arising from the shared resource model with EirGrid. For the time being we have not included any additional allowance (beyond those associated with the new compliance officer and maintaining an SLA) as there are a number of factors which could push SONI's costs either down or up:

- It may be the case that recharges for EirGrid staff cost more than the equivalent staff if employed by SONI and so with fewer recharges for staff costs envisaged in Options C and D, costs may come down;
- Conversely costs may be pushed up if there is a need for more staff at management level in Option C. However, at present we cannot say for sure as SONI has not provided UR with a staff resource plan. The SONI TSO business plan submission on manpower includes additional staff in areas such as communications and strategy but it is not clear whether they will form part of the MD office. A resource plan has been requested repeatedly from SONI but not provided pending re-structure in the EirGrid group. In any event in SONI TSO's 2020-2025 Price Control, the majority of manpower FTEs allowed are internal FTE's with a net figure of only 9.3 out of 116 being external FTE's (i.e. recharged from EirGrid). Therefore any cost increase from requiring SONI to have its own independent resources is likely to be marginal; or
- We would also expect an independent SONI Board and management team to actively work towards reducing operating costs going forward.

6.78 In regard to other costs, the governance options (with the exception of Option D) have been designed to ensure that SONI and EirGrid may generate benefit from economies of scale and synergies resulting from SONI's position in the EirGrid group. For example, even in Option C SONI may continue to avail of shared corporate services with EirGrid if approved by UR. Notably in Options A, B, and C

some services may also be shared with EirGrid plc e.g. control function, shared IT services and shared research and development (e.g. of control room tools) provided that there is appropriate oversight by SONI (and in the case of Option C approval by UR). Overall, to the extent that a loss of synergies may increase costs, we expect any such cost increase to be small in Options A-C.

6.79 In Option D it is difficult to assess the extent to which a loss of synergies may increase costs as limited information has been provided by SONI about the benefits of synergies and cost savings provided by the current arrangements. We have left this blank as to use the limited information we have could give a misleading picture. We would welcome further information from SONI on this aspect in response to this consultation.

6.80 UR accepts there will be some costs associated with the SONI Governance changes and these are not provided for in SONI's final price control determination but will be considered separately when/if SONI Governance changes are made. We are prepared to consider the need for a re-opener for these costs as part of any future licence modifications related to governance.

Table 3: Option A: SONI board with EirGrid NEDs

A	Option A Description	Unit	YEAR 2020-21	YEAR 2021-22	YEAR 2022-23	YEAR 2023-24	YEAR 2024-25	Totals £000's
1	One-Off Recruitment Costs	£'000	10					10
2	Independent Chair - (1 at £30k) ²⁶	£'000	30	30	30	30	30	150
3	Non Executive Directors - (1 at £15k each) ²⁷	£'000	15	15	15	15	15	75
4	Additional Managers - (3 at 15% above FD average) ²⁸	£'000	272	272	272	272	272	1,360
5	Additional Analysts - (1 at £79k FD average)	£'000	79	79	79	79	79	395
6	Total Governance Cost	£'000	406	396	396	396	396	1,990

Table 4: Option B: Independent SONI Board

A	Option B Description	Unit	YEAR 2020-21	YEAR 2021-22	YEAR 2022-23	YEAR 2023-24	YEAR 2024-25	Totals £000's
1	One-Off Recruitment Costs	£'000	10					10
2	Independent Chair - (1 at £40k) ²⁹	£'000	40	40	40	40	40	200
3	Non Executive Directors - (3 at £20k each)	£'000	60	60	60	60	60	300
4	Additional Managers - (3 at 15% above FD average)	£'000	272	272	272	272	272	1,360
5	Additional Analysts - (1 at £79k FD average)	£'000	79	79	79	79	79	395
6	Total Governance Cost	£'000	461	451	451	451	451	2,265

²⁶ The EirGrid plc's Chairperson's fees were equivalent to €21,600 per annum during the 2019 financial year. In all options Chair/NED costs include a small uplift for expenses and benefits in kind.

²⁷ This figure is based on EirGrid plc Directors fee which the EirGrid Annual Report for 2019 notes were equivalent to €12,600 each per annum during the year (2018: €12,600 each per annum). In this option we assume the NEDs on the SONI Board would also be EirGrid plc Directors and thus this would be an extension to their existing role.

²⁸ In Options A and B additional management and staff resources arise from the oversight functions that exist in A and B by virtue of reliance on EirGrid's shared resource model. They also cover the new compliance officer and any ongoing costs associated with managing the SLA.

²⁹ In Options B, C and D the Chair and other NEDs would be recruited by SONI and we have assumed that this may be at a slightly higher cost than rates achieved by EirGrid.

Table 5: Options C: Standalone SONI

A	Option C Description	Unit	YEAR 2020-21	YEAR 2021-22	YEAR 2022-23	YEAR 2023-24	YEAR 2024-25	Totals £000's
1	One-Off Recruitment Costs	£'000	10					10
2	Independent Chair - (1 at £40k)	£'000	40	40	40	40	40	200
3	Non Executive Directors - (3 at £20k each)	£'000	60	60	60	60	60	300
4	Additional Managers - (1 at 15% above FD average) ³⁰	£'000	91	91	91	91	91	455
5	Additional Analysts - (1 at £79k FD average)	£'000	79	79	79	79	79	395
6	economies of scale impact - cannot reliably be calculated at present	£'000						
7	Total Governance Cost	£'000						

Table 6: Options D: Standalone SONI no exceptions

A	Option D Description	Unit	YEAR 2020-21	YEAR 2021-22	YEAR 2022-23	YEAR 2023-24	YEAR 2024-25	Totals £000's
1	One-Off Recruitment Costs	£'000	10					10
2	Independent Chair - (1 at £40k)	£'000	40	40	40	40	40	200
3	Non Executive Directors - (3 at £20k each)	£'000	60	60	60	60	60	300
4	Additional Managers - (1 at 15% above FD average)	£'000	91	91	91	91	91	455
5	Additional Analysts - (1 at £79k FD average)	£'000	79	79	79	79	79	395
6	economies of scale impact - cannot reliably be calculated at present	£'000						
7	Total Governance Cost	£'000						

³⁰ In Options C and D additional management and staff resources cover the new compliance officer and any ongoing costs associated with managing the SLA. In these options there is no reliance on EirGrid's shared resource model, therefore no additional management and staff resources are needed to oversee the delivery of SONI functions via the shared resource model.

Cost of debt small company premium

6.81 Our draft determination for SONI TSO's 2020-2025 Price Control indicated that we did not think that NI customers should fund a cost of debt small company premium unless SONI can make appropriate changes to its governance arrangements to show that it is sufficiently independent of its parent to warrant a premium on the cost of debt. Nonetheless, we indicated that the governance consultation would include an assessment of whether, in consequence of any proposals on governance we make, a premium on the cost of debt is warranted. This would only be payable once the required changes in governance are made by SONI and verified by UR, e.g., via approval of a Compliance Plan.

6.82 In our TSO price control draft determinations, we considered SONI's proposal for a small company premium on the cost of debt benchmark that it had estimated. We said that we had concerns about the tension between SONI's proposal for a small company premium uplift, and SONI's governance arrangements which imply a high degree of integration with SONI's parent company EirGrid. We said that, given EirGrid's larger size and state ownership, and the lack of evidence from SONI on the case for a cost of debt premium for a notional TSO that enjoys this parent company arrangement, we proposed no uplift for the TSO's special characteristics or circumstances under the current ownership and governance arrangements. We also said that we did not think that NI customers should fund a small company premium unless SONI can make appropriate changes to its governance arrangements to show that it is sufficiently independent of its parent to warrant a premium on the cost of debt. For the purposes of our draft determinations, we did not include a small company premium uplift on SONI's cost of debt benchmark rate.

6.83 After the draft determinations were published further information was provided by SONI, including on its actual debt finance arrangements. We therefore decided to make a more direct estimate of the cost of debt for a notional TSO, drawing on evidence from SONI's bank finance arrangements and other relevant information. We did not consider it appropriate to consider a fully independent TSO (e.g., with no parent company or wider corporate ownership group) as this could make customers pay for a hypothetical fully independent TSO which they do not in practice benefit from. The options in this paper fall significantly short of a fully independent TSO outside of the EirGrid group.

6.84 Furthermore, such an approach would not be consistent with the allowance we provided for remuneration of a Parent Company Guarantee (PCG). This allowance was provided in part on the basis that the PCG might assist SONI in securing more efficient debt finance and provide some wider benefit for NI consumers in extreme downside scenarios. Under all options SONI would continue to have the benefit of a PCG from EirGrid plc.

6.85 In line with the policy position set out in our draft determinations, our 2020-25 TSO price control final determinations set the cost of debt allowance for SONI based on SONI's existing ownership and governance arrangements, before consideration of the effects of any changes arising as a consequence of our governance consultation.

6.86 We consider it plausible that, in principle, a fully independent TSO outside the EirGrid group could have higher debt finance costs than a TSO that is assumed to be integrated with EirGrid (or a similar organisation) and that these debt finance costs could, in turn, be higher than those which are allowed for under our TSO price control decision.

6.87 However, our governance proposals do not seek to establish a fully independent TSO outside the EirGrid group so this scenario is not relevant. SONI would remain part of the EirGrid Group in all options. Our current view is that our proposed governance changes would not give rise to a material incremental impact on the TSO cost of debt, above that which has been allowed for under the 2020-25 TSO price control decision. In particular:

- In the case of Option A (SONI Board with EirGrid NEDs) we do not consider that any increment on the cost of debt is warranted as this option creates a SONI board which is not independent from its parent, balancing this with other mechanisms to ensure that NI interests can demonstrably be taken into account through oversight by the SONI Board and that SONI Board and management are accountable to UR for how this is done.
- In the case of Option B (Independent SONI Board) we do not consider that any increment on the cost of debt is warranted as, while this option would create a more independent SONI Board, the decision-making authority of the SONI Board and management is augmented only in respect of a small independent management to provide oversight and assurance to the board, at a level and expertise to be determined by that board. This option therefore provides more independence for SONI than Option A but does not create a fully independent TSO outside of the EirGrid group.
- In the case of Options C and D (Standalone TSO) we do not consider that any increment on the cost of debt is warranted as, while both of these options would create a more independent SONI Board, and would augment the decision-making authority of the SONI Board and management as if SONI were a standalone company, SONI would remain within the EirGrid group. Although these options provide more independence for SONI than Option B, neither would create a fully independent TSO outside of the EirGrid group.

6.88 We would welcome any comments respondents have on this issue.

Estimated benefits

6.89 We do believe however that the benefits of a more independent and effective SONI TSO outweigh this additional cost. We calculate that every 1% reduction in costs incurred by SONI TSO would save consumers circa £550k p.a. based upon the portion of opex accounted for by TSO opex and system services in the 2018 regulatory accounts. Such a saving could arise (for example) through the challenge of costs being allocated to or imposed on SONI TSO by EirGrid, or the imposition of costs through a one size fits all approach either through enhanced specification or allocation of a more expensive shared resource now and in the future.

6.90 In addition, the new governance structures may also generate savings by allowing SONI the ability to develop and articulate its own service needs distinct from EirGrid plc, and the group structures in turn recognising SONI as a client distinct from all other group subsidiaries. At present SONI does not have sufficient decision making autonomy to reject a group service if it is unsuitable for SONI.

6.91 While SONI TSO's operating expenditure is small, its actions can significantly influence the costs faced by electricity market participants and the consumer. For example, the way SONI TSO designs and procures system services affects providers' ability to compete and the level of revenue available. SONI TSO should be ensuring the design, rules and/or processes for procuring system services maximise competition, where possible, and are fair and transparent. SONI TSO's Price Control for 2020-2025 is being designed to incentivise these outcomes but the outcomes of the governance review have a key role to play in ensuring that SONI TSO properly takes account of the needs of NI customers and is accountable and transparent.

6.92 The benefits which could be captured for NI electricity market participants cannot be quantified but are likely to be substantial. For example, the roll out of System Services is integral to meeting the challenge of connecting renewable generation to support the energy transition in both NI and Republic of Ireland. The Government of Ireland's published Climate Action Plan 2019 To Tackle Climate Breakdown includes the roll out of System Services under Action 24 of the list of actions annexed to the plan in the context of how Ireland will achieve its 2030 emissions targets.³¹ There is no corresponding plan yet for NI but it is likely that any future strategy will feature growth in the connection of renewable generation in NI in the coming years. Consequently, Systems Services costs are likely to grow substantially requiring a corresponding demonstration of value to consumers on both

³¹ See also Section 1.8 of the Government of Ireland's Electricity & Gas Networks Sector Climate Change Adaptation Plan Prepared under the National Adaptation Framework.

parts of the island. It is therefore important that SONI TSO's governance ensures that the interests of NI customers are taken into account in procurement decisions made by EirGrid and SONI TSOs. A small percentage reduction in System Services costs could realise a substantial saving.

6.93 A planning decision in NI requires NI benefit to be shown, and clear NI benefits articulated by SONI TSO will help new energy transition developments in the future get planning permission.

6.94 SONI's Price Control for 2020-2025 is designed to support NI's energy transition by supporting and incentivising SONI TSO to innovate and improve service quality in areas key to the energy transition such as stakeholder engagement and third party collaboration, whole system outcomes, and digitisation (open data) outcomes. Although the impact cannot be quantified at this time, we consider that the governance review outcomes will play an important part in ensuring that SONI TSO achieves the wider suite of outcomes envisaged by the Price Control.

6.95 An effective and timely energy transition will help ensure that NI can minimise risks and costs associated with climate change. No NI focused study is currently available which monetises the avoided costs to NI of taking climate change measures. The Government of Ireland's Climate Action Plan 2019 identifies business opportunities in a number of areas and there is no reason to consider that NI would be any different – in the energy sector these include renewables (including off shore renewables).

6.96 There will be other qualitative benefits arising from governance that cannot be quantified such as increased trust and confidence in SONI TSO arising from transparency accountability measures and better management of any conflict of interest, if any emerge. This will result in increased ability to meet NI government targets through better decision making by all within the NI energy industry.

Questions

1. Do you agree with our vision for good governance and our assessment of whether SONI meets this vision?
2. Do you agree with our analysis of the effectiveness of the existing licence in mitigating the majority of concerns raised within the CfE?
3. Have we adequately assessed the residual potential for harm given the current drafting of the Licence and statutory duties?
4. Are there other committees or working groups not identified in the paper that readers are aware of, that span both TSOs and that should be considered as part of any governance proposals?

5. Do you agree with the areas for discussion on which we have focused and do you agree with the consultation options we have proposed in respect of the creating an effective SONI Board? If so, which of the four options do you favour?

- ◆ **Option A: A SONI Board with EirGrid NEDs** which draws from the Non-Executive Directors of EirGrid plc considered by EirGrid to have 'NI background and standing' but which is supported by a small independent tier of dedicated managers specified within the Licence who oversee delivery of SONI licence obligations via the shared resource model with EirGrid.³²
- ◆ **Option B: An Independent SONI Board**, a fully independent board for SONI as defined by UKCGC and which is supported by a small independent tier of dedicated managers specified within the Licence who oversee delivery of SONI licence obligations via the shared resource model with EirGrid.
- ◆ **Option C: Standalone SONI within EirGrid Group (with provision for exceptions)** an independent board for SONI which is supported by a dedicated SONI management and staff team who deliver SONI licence obligations independently of EirGrid's shared resource model. With the approval of the UR some of these staff or services may be contracted from EirGrid and managed similar to third-party contracts with defined contracts, SLAs etc.
- ◆ **Option D: Standalone SONI within EirGrid Group (no exceptions)** a fully independent board for SONI which is supported by a dedicated SONI management and staff team who deliver SONI licence obligations independently of EirGrid's shared resource model.

6. Irrespective of the option chosen, do you agree with our proposals in respect of the SONI Board that:

- ◆ There should be a non-executive Chair of the SONI Board?
- ◆ The SONI MD should report to the SONI Board and not to the EirGrid CEO?
- ◆ The SONI TSO Licence should be strengthened to explicitly protect the interests of NI consumers and balance their

³² NB: This falls short of full compliance with the UKCGC.

interests with those of other stakeholders, and require the SONI TSO to maintain managerial and operational independence as appropriate from EirGrid?

- ◆ The SONI TSO Licence should also specify the scope and duties of the SONI Board ('matters reserved') and do you agree with those proposed duties?
 - ◆ The UKCGC makes reference to the need for specific sub-committees in exercising good governance. Should these sub-committees be adopted for the SONI Board and should an additional sub-committee be required to discuss and approve NI network policy, development and investment plans and proposals?
7. In Options B, C and D, should the SONI Board no longer be appointed by shareholders? If so, who should appoint the Board?
8. In regard to each option proposed, do you agree with our proposals in respect of SONI management and resources?
9. Irrespective of the option chosen, do you agree with our proposals in respect of other governance arrangements that:
- ◆ The transparency between the operations of EirGrid and SONI TSOs could be sufficiently improved through a SOA and its associated governance, or are there further proposals you would make?
 - ◆ Whilst not a public document for commercial reasons, do you believe it appropriate for UR to require SONI TSO to draw up and maintain an SLA to provide greater transparency and accountability for the services provided from across the EirGrid group to SONI TSO or from SONI TSO to the EirGrid Group?
 - ◆ Do you believe that the current EirGrid whistleblowing policy is effective to the extent it is applied to SONI or should SONI have its own published policy with suitable escalation routes to the SONI Board?
 - ◆ Do you agree with the need for SONI to publish a policy in respect of resolving any conflicts of interest that may arise, either between SONI and EirGrid TSOs, or between the interests of consumers within Republic of Ireland and NI?
 - ◆ Do you agree with our proposals for a specific Compliance Plan

in respect of the implementation of a more independent board and management, including an annual review by an independent Compliance Officer?

- ◆ Do you believe there is a need to amend the SONI TSO licence to require access on a non-discriminatory basis to UK companies who provide services to SONI through EirGrid joint procurement?
10. Do you have any views on our analysis of the cost and benefits of the various options?
 11. We ask SONI to provide any information available quantifying cost efficiencies and synergies which it says arise from the current governance structure
 12. Do you agree that none of our proposed options for governance changes would not give rise to a material incremental impact on the TSO cost of debt, above that which has been allowed for under the 2020-25 TSO price control decision?
 13. Does your view change on the above issues given our proposal to undertake a formal review of the effectiveness of any new proposals two years after implementation?

7. Assessment of the Options

7.1 The options proposed in the consultation paper build on each other as follows:

- Option A has a Board with EirGrid NEDs and a small independent tier of dedicated managers specified within the Licence;
- Option B has an independent Board and a small independent tier of dedicated managers specified within the Licence;
- Option C has both an independent board and a fully independent management and staff team. The UR may approve exceptions to the requirement for independent management and staff; and
- Option D has both an independent board and a fully independent management and staff team but without provision for exceptions to the requirement for independence.

7.2 The key difference between the options arises from how SONI satisfies us that sufficient independent attention has been applied to ensure that decisions and actions taken under its TSO licence are appropriate to the needs of Northern Ireland, its electricity consumers and energy policies. Specifically:

- In Option A (SONI Board with EirGrid NEDs), the SONI Board may overlap with that of EirGrid (through sharing of Non-Executive Directors), with potential conflicts of interest. To counter this, we will require a number of dedicated and appropriately senior staff within SONI to focus on key areas of SONI's TSO licence in conjunction with the other governance proposals that support and monitor the effective independence that apply to all options;
- In Option B (Independent SONI Board), SONI has a genuinely independent SONI Board to promote the interests of NI consumers, but with delivery of SONI licence obligations via the shared resource model with EirGrid. To support an independent Board and mitigate risks associated with this shared resourcing model we will also require a number of dedicated and appropriately senior staff within SONI to focus on specific areas of SONI's TSO licence in order to support the SONI Board of assuring itself of compliance with its licence.;
- In Option C (Standalone SONI with provision for exceptions) an independent SONI Board that is focused on the SONI TSO licence is supported by a dedicated SONI management and staff team who deliver SONI licence obligations independently of EirGrid's shared

resource model. However, to allow SONI TSO to take advantage of synergies which may be available from its position in the EirGrid group, this option makes provision for exceptions to the requirement for independence where SONI can make a case that this is in the best interests of NI consumers; and

- In Option D (Standalone SONI with no exceptions) an independent SONI Board that is focused on the SONI TSO licence, supported by a dedicated SONI management and staff team independent of EirGrid's shared resource model. To re-enforce this independence and promote transparency and trust, no synergies or sharing of EirGrid resources will be considered.

7.3 We will consider in our final proposals any Licence changes that may be necessary to give effect to our final decision.

7.4 Of the options set out, we prefer Options B and C for the following reasons:

- **Increased independence while maintaining scope for synergies:** Options B and C provides for an Independent SONI Board which is better placed to oversee its activities and risks than the Board envisaged in Option A. In Option C independence is strengthened with independent management and resource capable of fulfilling its licence obligations. Option C, while stipulating independence of resource, also provides for the UR to approve exceptions to this requirement, capturing synergies (where the case for these can be evidenced by SONI) whilst ensuring the best interests of NI consumers are achieved. Option D is not flexible in this respect and may make TSO coordination more onerous without delivering additional benefits;
- **Management of actual and perceived conflict of interest:** In Option A the potential for conflict of interest for those SONI Board Directors that are also on the EirGrid Board has a number of impacts:
 - ♦ **SONI TSO Culture:** It can increase fear of adverse consequences to staff of challenging the extent to which Group policies and plans meet the needs of the SONI TSO Licence, NI consumers and energy policies; and
 - ♦ **Trust:** A trusting relationship between SONI TSO and UR as well as wider stakeholders is more likely to emerge if the prospect for conflicts of interest at board level is reduced. This in turn can improve the quality of policies to support the move to a Low Carbon Economy.

7.5 In the following paragraphs we consider how each option addresses the issues we highlighted in Section 4 whilst maintaining trust, specifically:

- Inappropriately higher prices;
- Misalignment of NI policy and SONI approach to network development;
- Barriers to Competition; and
- Trust.

Inappropriately higher prices

7.6 As set out in Section 4, any increase in the costs of SONI TSO would lead to higher electricity prices for consumers.

7.7 The measures to address these issues are similar in each of the consultation options. However, we believe that as the options require greater independence of SONI they are likely to generate stronger incentives be more efficient (especially Options C and D), and hence lead to the lowest level of SONI TSO cost, and hence consumer electricity prices.

Transparency of SONI TSO Costs

7.8 The efficient management of costs relies on transparency for how those costs arise and relate to the key things a business needs to do to succeed. To provide this transparency, all options include a requirement that SONI TSO explicitly defines its cost boundary with the rest of the EirGrid group based on a fully costed and specified Service Level Agreement.

Gold Plating

7.9 The potential for increased costs of gold plating is reduced by SONI TSO having individuals of a suitable seniority, knowledge³³ and empowerment to understand whether the policies and actions of SONI TSO are appropriate. Our proposals deliver these in a number of ways:

- **Board Powers:** All consultation options require that the SONI Board explicitly approve (and have reserved powers in relation to) all policies and procedures used in the delivery of the SONI TSO Licence as appropriate for NI including the right to have SONI TSO specific variants to wider group policies;

³³ This knowledge will have to cover a number of areas, including understanding System Operations in general, the legacy transmission system in NI, and the specific requirements of NI energy policy.

- **Board Committees:** Each consultation option requires that the committees reporting to the SONI Board explicitly consider plans for development and operation of the SONI TSO network, alongside the policies and procedures for the discharge of SONI's TSO Licence;
- **SONI TSO Management:** Under Option A and B we have specified that SONI TSO must have dedicated management resources defined by UR within the TSO licence and capable of critiquing and challenging the engineering approach and plans adopted by SONI TSO, and the extent to which these need to differ from those proposed by the wider EirGrid group. The specification of such resources by UR under the TSO Licence is not required under Options C and D: the independent board will specify any such resources that it requires and which will be predominantly independent from that employed by EirGrid.

Challenge

7.10 The ability of SONI TSO managers and Directors to effectively challenge the costs allocated to SONI TSO is dependent on the culture within SONI. This ability to challenge is restricted if individuals perceive that such challenge will present a risk to their future career prospects and working relationships. This perceived risk is reduced in Option B and C by increasing the independence of the SONI leadership from the wider group. Option D eliminates the need for challenge as SONI resources for day-to-day operations are independent from EirGrid plc.

7.11 In addition to independence of the Board, the proposed arrangements include a number of measures to further support and protect the right of SONI TSO and its staff to challenge its strategies, policies and costs:

- **Whistleblowing & conflict resolution:** All consultation options require that SONI has its own policies and procedures for whistle blowing and conflict resolution.
- **Published Compliance Plan;** All consultation options will require SONI to prepare a compliance plan which describes how its managerial, resourcing and operational practices achieve its licence obligations. Such a plan will require the approval of UR and be published to achieve transparency and promote trust.
- **Board owns budget:** All consultation options require that the SONI Board has full ownership of the SONI TSO budget, and manages the business against that budget.

Misalignment of NI policy and SONI approach to network development

7.12 The development and operation of the network in NI is of critical importance to the interests of NI electricity consumers and the delivery of NI energy policy. Any shortfalls in how this is managed could lead to falls in the quality and reliability of electricity supplies, and difficulties in connecting new load or generation. The importance of these issues increases as we move towards a Low Carbon Economy, with any shortfall in this area making it more difficult and costly to connect new renewable generation, or to support increased load that may arise (for example) from electric vehicles and the use of heat-pumps for heating.

7.13 The Consultation proposals include specific measures to increase confidence that the state of the network is being managed appropriately. Specifically:

- **Board Committees:** Each consultation option requires that the committees reporting to the SONI Board explicitly consider plans for development and operation of the SONI TSO network, alongside the policies and procedures for the discharge of SONI's TSO Licence.
- **Independent Board:** Whilst all options increase the independence of the SONI Board and therefore provide greater assurance that SONI is acting to promote the interests of NI consumers, only Options B, C and D create a truly independent board as defined by the UKCGC.
- **SONI TSO Management:** Under Options A and B, we have specified that SONI TSO must have dedicated resources capable of critiquing and challenging the engineering approach and plans adopted by SONI TSO, and the extent to which these needs to differ from those operated by the wider EirGrid group. The specification of such resources by UR under the TSO Licence is not required under Options C and D: the independent board will specify any such resources that it requires and which will be predominantly independent from that employed by EirGrid.
- **Culture:** The above measures are supported by a culture where it is acceptable to challenge whether approaches developed outside of SONI TSO are appropriate and fit for purpose. This ability to challenge is restricted if individuals perceive that such challenge will present a risk to their future career prospects and working relationships. This perceived risk is reduced by increasing the independence of the SONI TSO Board and leadership from the wider group, without incurring the risks to coordination associated with Option D.

Barriers to Competition

7.14 The statutory duties of UR include a need, where appropriate, to ensure that competition is used in the interests of consumers. It is important then that any procurement run by, or on behalf of, SONI TSO is open, fair and effective.

Energy Transition and Trust

7.15 The transition to a Low Carbon Economy represents a change of paradigm for the electricity industry. This will require investment in, and changes to the configuration and operation of, the electricity transmission system managed under SONI's TSO Licence. Navigating these changes efficiently will require actions and decisions from both SONI TSO and UR.

7.16 UR's policy decisions need to be supported by objective analysis of how different low carbon scenarios impact the transmission system. This work analysis is best done by SONI TSO. Our proposals include a number of measures to ensure that such analysis is not de-prioritised by SONI (e.g., due to lack of resources), and that UR and SONI TSO develop a closer and more trusting relationship in this area. These include:

- NI Consumer Obligation;
- Compliance;
- SONI Independent Governance;
- Board Responsibility and Committees; and
- Whistleblowing and Conflict Resolution.

7.17 Success in this area is likely best achieved by a trusted partner that is able to be in a position to proactively engage with all stakeholders within NI and seek to develop the network innovatively and efficiently. This may result in differing approaches and attitudes to risk being adopted separately by EirGrid and SONI but whilst continuing to coordinate network development and operation. In our view an independent SONI is best placed to promote the interests of NI consumers in this regard, whilst this is increasingly demonstrated under Options B, C and D we are conscious that the ability to co-ordinate network operation and development diminishes with growing mitigating actions and costs increasing. This re-enforces our view that Options B and C are our provisional preferred options for the long-term benefit on NI consumers and stakeholders.

8. Responding to this consultation and next steps

Process and timetable

8.1 The consultation questions are set out in Section 6. Responses to this consultation should be received on or before 1700 on 11 June 2021. We will consider our final determination in light of the responses received to our consultation.

8.2 We aim to publish our final decisions by the end of October 2021 and will account for our findings and consideration of the consultation responses received as part of the determination.

8.3 The publication of the final decisions on SONI governance will, as necessary, be accompanied by a consultation on related Licence modifications to bring SONI's governance arrangements in line with the final decision. Any modifications would come into effect from March 2022.

How to respond

8.4 Responses to this consultation should be received on or before 1700 on 11 June 2021.

8.5 Responses can be sent in writing to or by emailing:

Roisin McLaughlin
The Utility Regulator
Queens House
14 Queen Street
Belfast
BT1 6ED

e-mail: Roisin.McLaughlin@uregni.gov.uk

and copying

e-mail: Electricity_Networks_Responses@uregni.gov.uk

8.6 Our preference is for responses to be submitted by e-mail.

Confidentiality

8.7 Please note that we intend to publish all responses unless marked confidential. While respondents may wish to identify some aspects of their responses as confidential, we request that non-confidential versions are also provided, or that the confidential information is provided in a separate annex.

8.8 As a public body and non-ministerial government department, UR is required to comply with the Freedom of Information Act (“FOIA”). The effect of FOIA may be that certain recorded information contained in consultation responses is required to be put into the public domain. Hence it is now possible that all responses made to consultations will be discoverable under FOIA, even if respondents ask us to treat responses as confidential. It is therefore important that respondents take account of this. In particular, if asking UR to treat responses as confidential, respondents should specify why they consider the information in question should be treated as such.

8.9 UR has published a privacy notice for consumers and stakeholders which sets out the approach to data retention in respect of consultations. This can be found at <https://www.uregni.gov.uk/privacy-notice> or, alternatively, a copy can be obtained by calling 028 9031 1575 or by email at info@uregni.gov.uk.

8.10 This paper is available in alternative formats such as audio, Braille etc. If an alternative format is required, please contact the office of UR to request.

Annex 1: Summary of non-confidential responses from Call for Evidence and UR response

1. UR would like to thank all stakeholders who submitted responses to the CfE on SONI governance. This section provides a summary of the non-confidential responses received, including the SONI response.
2. A total of 20 responses were received, 12 of which were non-confidential and 8 of which were confidential. Of the latter 6 were flagged as both anonymous and confidential. The level of responses which are both confidential and anonymous is unusual and many of these responses came from SONI employees both past and present. Given the confidentiality attached to them, we cannot put these responses into the public domain and stakeholders cannot see and evaluate them. Accordingly, we have not relied on the content of these responses in forming the proposals in this consultation paper. However, our review of these responses suggested largely similar concerns as the non-confidential responses. Also, where any of these responses suggested areas where further information could be useful, these were picked up either in further analysis by UR (e.g., analysis on the level of recharges between SONI and EirGrid) or in the form of questions included in the information request to SONI published on 29 January 2020.
3. The respondents to the CfE represent a good cross section of SONI's stakeholders as illustrated below.

SONI	1
CCNI	1
Electricity network companies	2 ³⁴
Wholesale market participants	1
Industry bodies	3 ³⁵
MLAs	2
Individuals	10 ³⁶
Total	20

Overview of non-confidential responses received and UR response

See spreadsheet published alongside the consultation paper

³⁴ NIE Networks and Mutual Energy Ltd. (MEL).

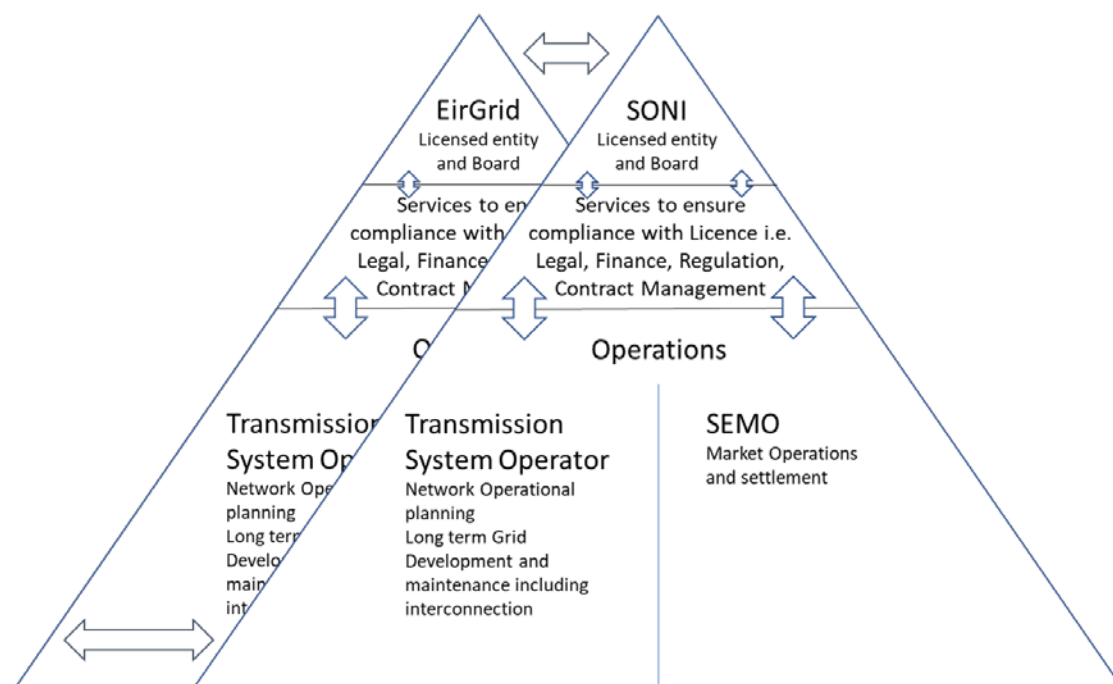
³⁵ One of which was confidential and not summarised here.

³⁶ Seven of which were confidential and not summarised here.

Annex 2: Summary of SONI's current governance arrangements

Purpose of this annex

1. A key aim of the governance review is to determine how SONI's governance structures work in practice. This annex identifies the key features of SONI's governance, drawing its evidence from SONI's own responses to the CfE and the subsequent information request.
2. We have tried to ascertain the nature of the relationship between EirGrid Group as the TSO licensed entity in Ireland, and SONI Ltd as the TSO licensed entity in NI. The annex is structured so as to discuss the level of protection and accountability afforded to NI consumers as per the levels of authority and accountability down through the organisation as depicted in the following figure:



3. This annex summarises SONI's governance arrangements with reference to:
 - SONI Board composition and duties
 - Resources in SONI to support the Board
 - Other elements of governance framework, including to promote transparency

SONI Board composition and duties

The composition of the SONI Ltd. Board

4. SONI advised UR that from 1 January 2020 the SONI Board was composed of two employees of EirGrid plc and one SONI employee. These are:
 - Aidan Skelly – Chairperson (Chief Financial Officer of EirGrid Group)
 - Rodney Doyle – Director (Chief Operations Officer and General Manager of SEMO)
 - Managing Director of SONI Ltd.
5. A number of observations can be made about this Board composition:
 - There are no independent non-executive directors (NEDs) on the SONI Board therefore SONI does not enjoy any of the benefits that independent NEDs could provide. For example, independent NEDs can bring a degree of objectivity to the board's deliberations, and play a valuable role in monitoring executive management.
 - The SONI Board has a majority of EirGrid employees and all SONI Board members are also members of the EirGrid executive team.³⁷ All have an executive management reporting line to the Group CEO, including the SONI MD. Consequently, there is no clear division of accountability and responsibilities between the SONI Board and the executive leadership of the SONI business. This means the Board may be less NI focused than it should be, a risk identified in 2016 when an agreement made between EirGrid and the SEM committee to ensure that the SONI Board would no longer consist of a majority of EirGrid employees so that it was able to be more clearly NI focused. The Board composition above breaks this agreement.
6. While our governance review was ongoing, two more appointments were made to the SONI Board in July 2020 and these are Dr Theresa Donaldson (who will also Chair the Board) and John Trethowan. Both are members of the EirGrid Board considered by EirGrid to have significant NI standing and Dr Donaldson is also Deputy Chair of the EirGrid Board. Subsequently, Tom Coughlan was also appointed to the SONI Board in November 2020. These appointments should strengthen the ability of the Board to hold management to account and ensure that the Board will be more NI focused in line with EirGrid's 2016 agreement with SEMC. However, these appointees are also members of the EirGrid Board, a circumstance which the UKCGC states could impair or could appear to impair, their independence. For the same reason, the revised Board's ability to manage

³⁷ <http://www.EirGridgroup.com/about/our-leadership/>

any conflict of interest between the needs of NI and Irish consumers could also be impaired or could appear to be impaired.

7. We also note a lack of transparency about SONI's constitutional documents. These do not appear to be in the public domain and so were requested by UR in the Information Request dated 31 January 2020. They were not provided by SONI.

Duties of the SONI Ltd. Board

8. The SONI Board's authority is cascaded down from the main EirGrid Board, through the Group CEO, to individual directors and managers in line with the delegated control framework (DCF) which sets out both the Board's responsibilities and the financial approval limits for individual managers and directors. The DCF is approved by the Group CEO, who therefore establishes the scope of authority of group subsidiary companies, including SONI.
9. An explanation of the scope of the SONI Board's authority was provided by SONI in response to UR's information request³⁸ in the form of Annex 2 of the DCF³⁹ which listed the following matters as reserved for the SONI Board. The SONI Board's authority is similar to other subsidiary companies in the group.
 - Appointment and removal of company auditors
 - Approval of bank mandates that are not in accordance with Group Treasury Policy.
 - Approval of all finance facilities (other than operating leases)
 - Approval of all guarantees or unlimited indemnities to be issued by the company where required
 - Approval of power of attorney of the company
 - Approval of use of the company seal
 - Approval where required under a commercial transaction with an external third party
 - Approval of financial statements
 - Approval in relation to pension arrangements
 - Approval of any other matters where required under statute from time to time
 - Approval required under its licence conditions.
10. From other information provided by SONI we also understand that the SONI Board:
 - Does not set the strategic direction of the company;

³⁸ See also Page 29 of the SONI response to the Call for Evidence which provided a list which did not include pensions nor the same level of clarity in respect of approval of commercial transactions.

³⁹ Published alongside the consultation paper.

- Does not monitor the development of or sign off the SONI business plan for the price control;
 - Does not have a formal role in SONI risk management;
 - Has no role in procurement decisions taken at group level and which incur cost for SONI;
 - Has no role in signing off the Cost Allocation and Recharge Policy;
 - Does not have responsibility for investment decision making which is carried out at a group level; and
 - Has no role in approving commercial transactions with another group company – as above it can only approve transactions with an external third party and therefore, we infer, not transactions with EirGrid plc or other group companies.
11. SONI have also told us that the EirGrid Board oversees the performance of all Group companies, monitors closely the financial performance of SONI, and ensures that adequate financial controls are in place, and that it is responsible for the overall strategic direction and performance of the group. In accordance with SONI's licenses, EirGrid has also provided Parent Company Undertakings to SONI. SONI's response to the CfE states that EirGrid plc also has a duty to ensure licence compliance by EirGrid plc and all subsidiaries.⁴⁰ However, SONI also states that the SONI Board is responsible for all items requiring approval under regulatory licence conditions. Therefore, the accountability and demarcation in responsibility is not fully clear.
12. From this information we conclude that the scope of authority of the SONI Board is extremely limited and therefore not designed to empower the Board to provide leadership for the company, set its strategic direction or provide oversight of the discharge of SONI's licence obligations.

Resources in SONI to support the Board

SONI management resources to support the Board

13. SONI does not have a dedicated management team which is responsible for SONI TSO functions and which reports to the SONI Board. Instead, EirGrid has adopted a 'cohesive all-island management structure' across both EirGrid and SONI operations and processes. Under this all-island operational model there is one Executive team, with the EirGrid CEO at the head.

Integrated management structure

14. The Executive Committee of EirGrid has responsibility for all key activities across the group and operates these through an integrated management structure. Chief Officers, or Executive Directors, therefore have full responsibility for each of their functional areas. The scope of the responsibility of Chief Officers covers

⁴⁰ SONI Response to the UR's Call for Evidence on SONI Governance, p.17.

collectively the full scope of SONI TSO business such as network operations, planning and company finances. Each functional area of the integrated management structure operates within the DCF.

15. Managers overseeing staff report to Chief Officers, who report to the EirGrid group CEO who in turn reports to the EirGrid plc Board.⁴¹ The SONI MD also reports to the group CEO. Management and staff are pooled across the group and carry out day to day tasks as allocated to them by a manager or a chief officer (SONI described this as a cohesive all-island team). We infer from this that managers/chief officers overseeing SONI business do not report to the SONI Board. Also, explicitly that day to day decisions about the management and allocation of resources available to SONI (staff, system or other resources) are taken without reference to the SONI MD, or the SONI Board.
16. Grid development and investment decision making is also undertaken by group-wide committees and not approved by the SONI Board but rather within the integrated management structure and ultimately the EirGrid Group Board:
 - Management Infrastructure Committee (MIC) provides support and assurance to the Transmission Investment Committee (TIC) regarding specific project proposals and underlying policies, which provide the foundation for transmission investment decisions across Ireland and NI. It is able to authorise some projects and refer larger projects to the TIC. SONI managers and staff attend meetings 'as appropriate' but it is not clear from SONI's response who the standing members of the committee are;
 - Transmission Investment Committee ensures good governance with respect to network capital investment decisions and provides oversight in the monitoring and control of network development across NI and Ireland and refers larger projects in excess of its authorisation to the Grid Infrastructure Projects Committee. Again, SONI's response fails to detail who are members of that committee;
 - Grid Infrastructure Projects Committee (GIPC) assists the EirGrid plc Board in determining the general policy and strategy in relation to Grid development. The GIPC consists of four members of the EirGrid Board with relevant Executives invited as required.
17. From this information we conclude that SONI's management structure is not designed to ensure that the SONI Board can oversee how SONI's licence responsibilities are being discharged. That oversight is being provided at EirGrid plc Board level.

⁴¹ As per response submitted by SONI in response to the information request. As regards reporting lines this is identical in effect from the previous group structure.

Other elements of governance framework, including to promote transparency

SLA

18. There are no Service Level Agreements in place such that the SONI Board could approve or monitor prescribed performance levels and value for money from a shared management organisation.

SOA

19. At acquisition a System Operator Agreement (SOA) was put in place under a Licence condition pertaining to both SONI and EirGrid as both TSO and SEMO. SONI's response to the CfE notes that it told UR in 2013, that the SOA arrangements had been 'internalised.' At the time no explanation was given of what this meant in practice, including for SONI's Licence compliance with the SOA licence condition. In its response to the information request of the 29 January 2020, SONI does not directly establish how this is in compliance with the licence condition. SONI considers that it is "confident it fulfils the obligations which the SOA is designed to enable it to fulfil, through the cohesive team structure". It states that it believes the arrangements are quite different today from those at acquisition when the SOA was put in place and emphasised that the integrated management and governance structure means that 'decisions can be taken more seamlessly today'. This would suggest that SONI believes that somehow the relevant Licence requirement is redundant – it is not.
20. The SOA remains SEMC policy and has remained unchanged, following review by the TSOs themselves from SEM to new SEM. It requires an interface between the two TSOs rather than a single team as appears to be the position being communicated by SONI to UR. UR does not accept that such internalisation fulfils the requirement of the licence condition.

Cost allocation and recharge policy

21. SONI's response to the Call for Evidence acknowledges the importance of the Group Cost Allocation and Recharge Policy in SONI's corporate governance arrangements, noting that its purpose is to ensure a fair and supportable basis for cost attribution across the group. While it was developed jointly by EirGrid and SONI finance teams, the SONI Board does not appear to have any role in scrutinising it or in signing it off. Many of the allocations within the policy are also subject to management's view of apportionment, or a simple 3:1 allocation of costs between EirGrid and SONI.
22. We have seen no evidence of a performance management or approval process in place to ensure that SONI is provided with appropriate costs and service to allow it to judge whether EirGrid is acting in a manner which

protects the interests of NI. The overall impression is that SONI is a 'price taker' under the Group Cost Allocation and Recharge Policy.

Risk management

23. SONI's reply stated that SONI Ltd. risks are identified and mitigated through the management structure and captured within the integrated framework of EirGrid's top-down/bottom-up approach to risk management. The reply also stated that risk registers are captured and held by SONI's compliance and assurance officer⁴² which enables him/her to provide necessary assurance concerning the management of SONI risks.
24. This information is consistent with information on risk management provided to UR within the SONI business plan for the 2020-2025 price control period. From this, we can see that SONI risks can be escalated upwards and that any risks so escalated will be reviewed annually by the EirGrid Board risk committee and approved by the EirGrid Board. However, we have no assurance that a holistic picture of risks facing the SONI business is maintained and that these risks are monitored and managed by SONI.

Management of Conflict of interest and whistleblowing

25. SONI did not describe the arrangements in place to manage conflicts of interest in the Group. EirGrid currently have a whistleblowing policy that extends across the Group and a copy was provided. That policy includes an escalation process including reference to the Group Head of Audit and Compliance, HR Directors and CEO, extending to Chair as necessary. The policy also includes reference to external 'Prescribed Persons' including UR and is published on the SONI website. Instances of whistleblowing are reported as they arise by the Group Head of Audit and Compliance to the Audit and Risk Committee of the plc Board. We have seen no evidence to suggest that the policy is signed off by the SONI Board; the SONI Board appears to have no role in respect of it.
26. Section 2.7 of SONI's response to the CfE references a governance review centring around conflicts of interest in the EirGrid group which took place in the run up to ISEM implementation. SONI notes that following this review EirGrid voluntarily ensured that the CEO of EirGrid no longer sat on the SONI Board (although he continues to be a member of the SONI's UK holding company). We note that the driver for this review was the new responsibilities⁴³ envisaged for EirGrid and SONI as TSOs in the ISEM. In particular market participants raised concerns about the (perceived) scope for conflicts of interest to arise between the EirGrid group carrying out these

⁴² UR are aware that the SONI compliance and assurance officer role is carried out by the EirGrid Group Compliance and Assurance Officer

⁴³ These were in the Capacity Market, Balancing Market (as part of the Electricity Trading Arrangements), and System Services.

functions and its activities in the ownership/development of interconnection. Given the focus on ISEM, the review did not consider any potential conflicts of interest between SONI TSO and EirGrid TSO. Therefore, UR signalled that it would conduct a review of SONI's governance (the present review).

EirGrid 'best practice' governance arrangements

27. SONI's response to the CfE sets out that EirGrid seeks to comply with best practice in corporate governance such as the UKCGC and notes a number of features of group governance (such as the reservation of matters to the EirGrid plc Board) which it considers in accordance with best practice. Also, that these arrangements help ensure that 'the group operates as a cohesive organisation and that controls are adequate and appropriate across the group.'⁴⁴
28. The responses to the CfE indicate that the EirGrid model is a centralised approach characterised by a strong plc Board, a limited Board at subsidiary level, a range of corporate policies applicable to subsidiaries, and pooling of subsidiary resources in an integrated management structure reporting upwards to the EirGrid plc Board. In the context of Republic of Ireland where a number of companies in the group hold licences all regulated by CRU, a centralised model would appear to make perfect sense. Therefore, in EirGrid's governance we recognise many best practice features of governance such as the composition of the EirGrid plc Board with its majority of independent non-executive directors.
29. However, we are not concerned with whether EirGrid's governance is best practice but with SONI's. In that regard, SONI is unlike other companies in the EirGrid group. It is incorporated in another jurisdiction, separately regulated by UR, and funded by a separate set of customers – those in NI. In these circumstances the balance that EirGrid has struck between control of SONI and driving synergies through a shared resource model, and on the other the autonomy SONI needs to operate as an independent legal entity is the key issue. SONI is separately licensed and regulated in another jurisdiction such that it acts in the interest of and is accountable to NI consumers. This does not call into question in any way the efficacy of EirGrid's governance structures as applied to the rest of the group, all of which sit in a common Irish legal and regulatory context.

⁴⁴ P. 17 of SONI's response to the Call for Evidence.

Annex 3: Regulatory Precedents

European Directives

1. Across Europe, current regulation of electricity System Operators is based on the Electricity Directive which formed part of the 3rd Energy Package (2009/72/EC).
2. The key sections of this package and, in particular, those related to governance of the Independent Transmission Operator or Independent System Operator are re-stated almost word-for-word in the Electricity Directive which forms part of the Clean Energy Package (2019/944/EC).
3. The Directives require that either an Independent Transmission Operator, where the same entity owns and operate the transmission system, or an Independent System Operator, where ownership and operation of the transmission system are performed by different entities, is established.
4. In the context of NI, NIE is the transmission system owner with SONI acting as the Independent System Operator (ISO).
5. As an ISO, SONI is responsible for “collection of access charges, congestion charges, and payments under the inter-transmission system operator compensation mechanism [...], as well as for operating, maintaining and developing the transmission system, and for ensuring the long-term ability of the system to meet reasonable demand through investment planning. When developing the transmission system, the independent system operator shall be responsible for planning (including authorisation procedure), construction and commissioning of the new infrastructure.” (2019/944/EC Art. 44(4))
6. The transmission system in question is the NI system, the Republic of Ireland system lies within a separate Member State, with a different transmission system owner and operator. As a result, SONI's obligations under the Directives apply solely to the NI transmission system.
7. As a transmission system operator, SONI “shall be equipped with all human, technical, physical and financial resources necessary for fulfilling their obligations under this Directive and carrying out the activity of electricity transmission.” (2019/944/EC Art. 46(1))
8. The Directives enforce separation between the ISO, and any entity which performs any of the functions of generation or supply. The EirGrid Group does not undertake any activities that could be considered generation or supply. However, it is worth noting that these provisions apply to concerns covered by the Directives are focused on vertically-integrated undertakings (as defined in the Directive) and the EirGrid Group would not be considered as such an

undertaking. As such, there is no legal restriction in terms of SONI being part of the EirGrid Group. Nevertheless, SONI, as a TSO, does need to have its own Supervisory Board (Art. 49) and compliance programme and Compliance Officer (Art. 50). However, it should be noted that the Supervisory Board is not involved in day-to-day operation of the TSO but only acts to protect the long-term financial interests of shareholders.

9. The Directive does make clear that the TSO must ensure “non-discrimination as between system users or classes of system users, particularly in favour of its related undertakings” (Art. 40(1)(f)). This would clearly apply to the competing interests of Irish and NI system users and customers.

Current SONI Licence Conditions

10. Condition 12 (Independence of the Transmission System Operator Business) of the SONI Transmission System Operator licence requires it to maintain “the full operational independence of the Transmission System Operator Business”. In particular, that the “Transmission System Operator Business is provided with the premises, systems, equipment, facilities, property, personnel, data and management resources that are necessary for its efficient and effective managerial and operational independence from any Associated Business”.
11. Condition 12 places significant limits on any Associated Business having access to the premises, systems and equipment of SONI. It also requires, in line with the Electricity Directives, SONI to produce a Compliance Plan and appoint a Compliance Officer to monitor, investigate and report on SONI’s compliance with the conditions which ensure the independence of the Transmission System Operator Business.

Treatment of the Electricity System Operator (ESO) in GB

12. In November 2015, GB ministers called for greater independence for the ESO. This was in response to the evolution of the activities being performed by the ESO whose role was expected to continue to grow in importance. This created a need to “carefully consider the governance of the ESO, to ensure that there is sufficient focus on its important role and to address any actual or perceived conflicts of interest between National Grid’s ESO functions and other business interests, such as the electricity TO and the electricity interconnectors”.
13. In January 2017, OFGEM issued a consultation paper on “proposals regarding the structure of the ESO within National Grid plc and, in particular, the need to mitigate any actual or perceived conflicts between National Grid’s role as ESO and other roles such as its ownership of the transmission network in England and Wales.” Following responses to this consultation, OFGEM produced a detailed proposal and from this National Grid produced a

counter proposal. Following an extensive programme of work and consultation involving National Grid Electricity Transmission (NGET), BEIS, OFGEM and the wider industry, this National Grid proposal formed the basis of the separation of the ESO into a separate company within the National Grid Group and the separation of the licences for the transmission owner and transmission system operator. This process was completed on 1 April 2019.

14. The key separation arrangements are:

- The ESO has a separate board with 3 National Grid Board Members, 3 Sufficiently Independent Directors⁴⁵ and a Chair who is the Director of the ESO.
- In principle, all ESO staff will be employed by the ESO with managers and executives incentivised on ESO metrics. (There is an exception for a small number of 'dual fuel' staff who will work for both the ESO and the gas SO).
- The ESO is physically separated from other parts of National Grid's business.
- Transactional services are shared while strategic services will be shared under a business partner arrangement.
- The ESO has its own regulatory capability.
- The ESO has a distinct visual identity to help to separate its culture from the rest of National Grid.

15. The Sufficiently Independent Directors are appointed by ESO as the licensee but Standard Condition B22 of its licence requires any appointment, removal or resignation to be notified to the Authority.

16. The key arrangements relating to physical, legal and staff separation were placed into ESO's licence as part of Special Condition 20, "Business separation requirements and compliance obligations, and conduct of the System Operator in performing its System Operator Functions". In addition, Standard Condition B22 of the Transmission Licence was modified to increase the number of sufficiently Independent Directors to three.

17. The National Grid proposal also included a separate SO Executive Committee (SOEC) that will manage day-to-day operations of the ESO and an independent compliance oversight committee chaired by one of the ESO Board Sufficiently Independent Directors.

18. Residual stakeholder concerns will always remain while the ESO remains part of the National Grid Group. OFGEM has taken responsibility to monitor the separation closely with the intention of undertaking a review in 2020-2021 "to see how effective the measures are in delivering the benefits of separation".

⁴⁵ As defined in Standard Condition B22 of the Transmission Licence: i.e. be a natural person with sufficient skills for the role and no executive position within the licensee's business. Unless authorised by the Authority, it should not be an employee of, nor have a material relationship with, the licensee or any of its associates

19. In January 2021, OFGEM issued a revised consultation paper on GB System Operation. This has four key findings:

- “Finding 1: Net Zero requires a step change in whole-system co-ordination and planning”;
- “Finding 2: The system operators are uniquely positioned to play a critical role in achieving net zero”;
- “Finding 3: An Independent System Operator (ISO) with enhanced functions will be required to enable and facilitate an integrated, flexible energy system”; and
- “Finding 4: We believe there are several alternatives to the current model that would be better suited to delivering net zero at least cost for consumers”.

20. As part of Finding 3, OFGEM have acknowledged issues with the alignment of shareholder and consumer objectives in their recent consultation paper on GB System Operation⁴⁶. This notes that System Operators have a “limited appetite for risk taking [that] may prevent proactive leadership in complex areas”. This is driven (in part) by a “reputational risk” that external stakeholders may take issue with the System Operator’s view on how the operation and governance of the energy system should evolve to meet new challenges – such as those arising from the transition to a Low Carbon Economy.

21. The specific remedies that may arise from Finding 4 have not been detailed in entirety, but include considering alternatives to a shareholder owned limited company as the System Operator.

OFWAT: Board leadership, transparency and governance principles

22. OFWAT published its board leadership, transparency and governance principles in 2019 and these have become part of the licences for the largest regulated water companies and licensed infrastructure providers. While these principles cover a different industry, many of the issues addressed by these principles will apply to SONI.

23. These principles were updated as companies largely complied with the earlier principles (introduced in 2014), the corporate behaviour of some companies, along with significant service failures, has damaged trust in the sector. Therefore, in April 2018, OFWAT’s Chief Executive wrote to companies setting out a programme of work to enable and challenge companies to rebuild legitimacy and put customers at the heart of their businesses of which these principles form a part.

⁴⁶ Review of GB energy system operation, Ofgem, 25 January 2021

24. The document sets out four key objectives which are elaborated by more detailed provisions.

- **Purpose, values and culture:** The Board of each utility “establishes the company’s purpose, strategy and values, and is satisfied that these and its culture reflect the needs of all those it serves.”
- Whilst seemingly “woolly”, OFWAT considered there needed to be clear recognition that water companies have a special responsibility to work as diligently for their customers as for their owners which this objective is intended to accomplish.
- **Standalone regulated company:** The Board will be effective with full responsibility for all aspects of the utility’s business for the long term.
- **Leadership and transparency:** The Board’s leadership and approach to transparency and governance should engender trust in the utility and ensure its actions are accountable.
- **Board structure and effectiveness:** The Board and its committees must be competent, well run and have sufficient independent membership. This will ensure that they can make high quality decisions that address diverse customer and stakeholder needs.

25. The aim of this proposed objective is to bring a new quality dimension to board decision-making by asking boards to show how they address customer and stakeholder needs, and diversity.

26. This objective also formalises the arrangements OFWAT have in place to meet with all non-executive directors prior to their appointment, to ensure a clear understanding of the special responsibilities that attach to non-executive directors of a regulated water company.

27. The “Board structure and effectiveness” objective contains a number of key provisions:

- Independent non-executive directors should be the largest single group on the board.
- The Chair must be independent of management and demonstrate objective judgement throughout their tenure
- There must be a clear understanding of the responsibilities attached to being a non-executive director and proposed, final candidates for new non-exec appointments must meet with OFWAT before a formal appointment is made.
- There should be a majority of independent members on the audit, nomination and remuneration committees and the audit and remuneration committees must be independently led.

Regulation of National Grid in the USA

28. National Grid have acquired a number of utilities in the North-eastern states of the USA. These utilities are typically in the networks part of the energy utility

value chain - with prime responsibility for the transmission and distribution of electricity and gas.

29. National Grid USA now own and operate electricity transmission and/or distribution facilities across the following states⁴⁷, each of which has its own utility policies, laws and regulator:

- New York;
- New Hampshire
- Rhode Island; and
- Vermont

30. This gives rise to a tension between differing State policies, and the efficiency opportunities from National Grid (for example):

- Standardising the design and engineering of the networks it owns.
- Optimising its field workforce, including allowing workers from one state can work on the network in a neighbouring state.

31. In response to concerns expressed by State regulators, National Grid introduced the concept (and role) of Jurisdictional President. These roles (one for each State) are pitched at a senior level in the Company (Senior Vice President), reporting directly to the Group Director USA. The President, supported by a small core team, would be the primary interface between the Company and the State Legislators and Regulators for activities in the State in question. The Jurisdictional Presidents can also be Board Directors of (and in fact chair) their respective jurisdictional corporate entities within National Grid USA. The Jurisdictional Presidents would be the public face of National Grid in their respective State and would be directly involved in promoting State-specific energy initiatives (e.g. energy saving, business support etc.). Being part of the same leadership team as the Group Director's other direct reports allows them to ensure coordination and an appropriate State focus to distribution operations within the State. For example, another parallel direct report would be the Senior Vice President for Strategy and Regulation through whose team's regulatory ratemaking and tariff setting would be carried out.

32. Although, the Jurisdictional Presidents do not have direct line management of the system planners, maintainers and tariff setters, they take ultimate responsibility for all that happens (electricity-distribution wise) in the State. They could be regarded as the "directing mind" and their colleagues are required to take State mandates into account in flexing or modifying the approach taken by their teams to ensure compliance with those mandates. In practice this means that regulators and legislators are given comfort that State-specific regulatory and legislative priorities are being given suitable prominence and are acted upon by National Grid.

⁴⁷ <https://www.nationalgrid.com/group/about-us/what-we-do/us-principal-operations>

Governance of Elia in Belgium

33. The Belgian Energy Code is particularly prescriptive in the definition of the governance of the System Operator. The key regulations are set out in Article 9 of the “la loi relative à l'organisation du marché de l'électricité” of 29 April 1999 (as revised).
34. The SO's board must be comprised wholly of non-executive directors of which at least half must be independent. The board should have at least audit, remuneration and corporate governance committees. These should be composed exclusively of non-executive directors and a majority of their members should be independent.
35. The State can, by Royal Decree, appoint two representatives to the SOs board who will sit in an advisory capacity. These representatives have the ability to appeal any decision of the board to the Minister within four working days of the decision (or when they become aware of such decision). The appeal is suspensive and if the Minister does not annul the decision within eight working days, it becomes final.
36. The board appoints the management committee of the SO, including its president and vice-president. These latter two sit on the board of directors in an advisory capacity. The division of powers between the board and management committee is set out at a high level: with the board responsible for high level direction and the management committee for day-to-day management of the SO.
37. When the terms of office of board members is renewed, there is a requirement to achieve and maintain the linguistic balance, i.e. between French and Flemish speaking members.

Governance of NIE Network Businesses (Northern Ireland)

38. The physical electricity network assets in NI are owned, maintained and operated by Northern Ireland Electricity Limited (NIE) under separate licences for Distribution and Transmission. In each case these network businesses are owned by the Electricity Supply Board which:
 - Also owns, maintains and operates the electricity network assets for the Republic of Ireland; and
 - Is 95% owned by the Government of Ireland.
39. The licences for NIE Transmission and NIE Distribution include a number of measures to ensure that protect the interests of electricity consumers in NI, and ensure that NIE Networks remain independent. These include:
 - **Independent Board:** Condition 3A of the relevant licences requires that each

licencee:

“ensure that its board of directors comprise a majority of independent non-executive directors who are persons of standing who individually possess:

- (i) relevant experience and knowledge of the energy industry; or*
- (ii) relevant experience of any other regulated industry; or*
- (iii) substantial private sector commercial or financial experience gained at board level (or equivalent) in another organisation of comparable size and standing of the Licensee*

Providing that at least one independent non-executive director must possess relevant experience and knowledge of the energy industry”

- **Managerial and Operational Independence:** Condition 12 of the relevant licences require that each company *“maintain the full managerial and operation independence of the relevant⁴⁸ Business from any associated business”*. This would force separation from the similar network businesses of ESB that own, maintain and operate electricity networks in the Republic of Ireland.
- **“Whistle Blow”:** Paragraphs of Condition 12 requires the licensee to notify the Authority⁴⁹ if it is being forced to act other than in compliance with its licence:

“Where and to the extent that a holding company exercises its corporate governance role in relation to the Licensee, unless that exercise falls within the relevant part of the Compliance Plan permitting such exercise in specified circumstances, the Licensee shall within 3 days of such exercise notify the Authority of that fact and provide such other information regarding such exercise as the Authority may require.”

40. The measures in the NIE licences are similar to those proposed in Option D.

Whistleblowing Precedents

⁴⁸ This is stated as *“Distribution”* in the Distribution Licence, and as *“Transmission”* in the Transmission Licence

⁴⁹ Northern Ireland Authority for Utility Regulation

Whistleblowing Protection in NI Employment Law

41. NI has whistleblowing protection arrangements in place in employment law through The Public Interest Disclosure (Northern Ireland) Order 1998 (PIDA)⁵⁰, which amends the Employment Rights (Northern Ireland) Order (1996) (together referred to as the applicable legislation below) and came into full force in 1999. The applicable legislation protects workers who make a disclosure and includes the following:

- **Defines what a “qualifying disclosure” is:** This sets the criteria for what disclosure types can qualify for protection, and includes criminal acts, failures to meet legal obligations, environmental failures, health and safety failures, miscarriages of justice, and deliberate concealment of any of these categories. The worker must have a reasonable belief that the disclosure meets the qualifying criteria. These failures are not limited to the UK, but do not qualify if the person making the disclosure commits an offence by making it;
- **Defines to whom a disclosure can be made:** This includes employers, legal advisers, prescribed persons (i.e. as prescribed by way of an order made under the applicable legislation by the relevant NI Department and includes UR in respect of certain specified matters), and in some cases Ministers. The applicable legislation sets out conditions for all other cases, which includes criteria such as disclosures being in good faith, believed to be substantially true, and not made for personal gain. It also sets out escalation routes if an initial disclosure has already been made;
- **Defines who qualifies as a “worker”:** PIDA is part of employment law and protects workers in a broader sense, as it expands the definition of a worker from the Employment Rights Order. It is extended to cover contractors, third party workers, health providers, trainees and those on work experience; and
- **Sets the protections:** This establishes that a worker cannot be subjected to a detriment by any act, or any deliberate failure to act, by their employer on the grounds of having made a protected disclosure. Any dismissal based on a protected disclosure having been made constitutes unfair dismissal. Workers may take complaints in this area to employment tribunals.

EU Directive and Interaction with NI Legislation

42. PIDA (and its equivalent for GB) meant that the UK was viewed as having comprehensive protections for whistleblowers when the EU drafted a Directive on the same topic. The Commission was successfully lobbied to write a Directive in the wake of the Panama Papers and Cambridge Analytica information disclosures. This was approved in April 2019, and published as EU Directive 2019/1937⁵¹, with Member States given two years to implement.

⁵⁰ <https://www.legislation.gov.uk/nisi/1998/1763>

⁵¹ <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019L1937&from=en>

43. Directive 2019/1937 defers to protection measures already in place in other sectors with pre-existing arrangements and EU acts. It also does not specifically cover employment law, and therefore has some notable differences to PIDA. If fully adopted in UK, it would mean legislative changes that include:

- **Internal channels for whistleblowers:** Under Articles 7-9, private legal entities with 50 or more employees must set up a procedure for reporting of breaches internally. The channel established can be shared with other companies up to a company size of 249. These internal channels must acknowledge receipts of reports within seven days and provide the whistleblower with feedback within three months of the acknowledgement of receipt. These requirements are absent from PIDA;
- **Protected persons:** PIDA is part of employment law and protects workers in a broad sense that includes contractors, third party workers, health providers, trainees and those on work experience. Article 4 of 2019/1937 has a broader definition that includes, but is not limited to, civil servants, shareholders, volunteers, self-employed people, and those working under direction of contractors. The Directive states that protection measures should apply in pre-employment and post-employment timeframes. It also has a wider scope beyond the whistleblower, which includes connected persons (e.g. family, colleagues), facilitators who support the whistleblower, and any other legal entities connected to the whistleblower in a work-related context; and
- **Scope of protection and penalties:** The Directive goes beyond stating that a worker is protected from detrimental acts. It sets out a set of support measures that must be made available, including advice, assistance and in some cases legal aid, as well as protection from retaliation. This is notable for protections when cases are brought to court – in such cases it is presumed that any detriment suffered was a form of retaliation, and therefore the burden of proof rests on the defending party, namely the employer (see Articles 20 and 21). It also sets out the conditions where a public disclosure still attracts protected status.
- Under Article 23, the Directive also obliges Member States to apply penalties to any parties that hinder disclosures being reported or retaliate against the whistleblower, but equally apply penalties to those making false disclosures and recover resulting damages.

Financial Incentives and US Whistleblowing Protection in the Financial Sector

44. Neither EU Directive 2019/1937 nor PIDA set a financial incentive for whistleblowing (although, under Article 20 of the Directive 2019/1937, member states have the discretion to provide for financial assistance for whistle blowers in the framework of legal proceedings).

45. The US includes such “qui tam” clauses in several Acts that include the False Claims Act and Dodd–Frank Wall Street Reform and Consumer Protection Act. The latter was brought in in 2010 to regulate the US financial sector after the Great Recession does include financial reward. This Act includes protections for whistleblowers (job protection and guarantee of confidentiality),

and incentives (whistleblowers can be awarded 10-30% of collected sanctions in cases of greater than \$1 million). This has led to some high-profile and sometimes controversial cases (e.g. Bradley Birkenfeld, a whistleblower of UBS international tax fraud in Switzerland, who was awarded \$104m in 2012. Between initial disclosure in 2007 and payment award, he served two and a half years in prison for conspiracy to defraud the United States through advising on tax evasion) and the growth of an industry that advises and invests in achieving pay outs (including legal practice, private investigators, and investors in individual cases).

46. In 2014, the PRA and FCA conducted a study⁵² to look into whether or not to introduce financial incentives for UK whistleblowers. The study found that the Dodd-Frank Act had not led to agencies seeing “significant increases in either the number or the quality of reports from whistleblowers”. The study concluded that financial incentives would not encourage whistleblowing, or significantly increase integrity and transparency in financial markets.

⁵² <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/financial-incentives-for-whistleblowers.pdf?la=en&hash=04316B710E99A192FD08E9D8AF2635473EFCF071>

Annex 4: SONI Upfront service expectations

Extract from SONI Price Control Draft Determination Annex 4, Technical annex Evaluative Performance Framework

- 1.1 Our guidance documents would specify a set of upfront service expectations. These would set out our position on what a good TSO would do and/or achieve in relation to its activity under each service area, taking account of each service area's influence on, and contribution to, the SONI outcomes.
- 1.2 They would play a central role in the annual evaluation of SONI performance, by providing information on the baseline level of performance expected from SONI: i.e. the level of performance that does not qualify for a financial reward or penalty.
- 1.3 The upfront service expectations are not intended to be a comprehensive description of the role and requirements of SONI in each service area or to act as a replacement for licence obligations (although we anticipate that some expectations may require new licence conditions). The focus is on issues and aspects identified for the purposes of the evaluative performance framework within the SONI price control.
- 1.4 There would be separate service expectations for each of the service areas, where relevant. The upfront service expectations would be revised over time in light of learning from experience, and adaption to new developments.
- 1.5 We recognise that there are interactions between the upfront service expectations and the ex-ante cost allowances and caps we are proposing for SONI for the 2020-25 price control. While the upfront service expectations do not fully specify the set of activities that SONI must carry out, or provide a detailed and comprehensive set of required service levels, they do imply targeted requirements on SONI to qualify for baseline performance levels.
- 1.6 We are keen to receive feedback from stakeholders if there is evidence that those cost allowances and caps are too low, or too high, for the upfront service expectations (within the wider context of our draft determinations).
- 1.7 We recognise that scoping work to meet some of these service expectations is likely to represent a step change over and beyond TSO activity SONI undertakes today. For example, some of the service expectation examples relate to a whole system way of working and strategy development which SONI does not currently seem to undertake.
- 1.8 We have, therefore, proposed an uplift to the baseline of allowances (see cost allowances appendix) to support SONI in scoping out such work. We ask for more detailed views from SONI and stakeholders as part of DD

response on the level of the uplift required.

- 1.9 We have drafted the upfront service expectations based on stakeholder views (e.g. SECG), our own experience of issues, and relevant information from other regulators (for example, OFGEM's ESORI roles and principles in particular where these align with ours and stakeholders' views). We also asked our consultants GHD to have a look at some international case study practice elsewhere (see annex on whole system planning), some of which could be described as genuinely innovative. The point of this is not to prescribe deliverables for SONI but to present some innovative practice elsewhere, some of which broadly fits within our service expectation themes below relating to the energy transition.
- 1.10 We think SONI should be taking a more whole system collaborative and coordinated approach to working with various stakeholders, including NIE Networks. As well as considering how it can improve its tools and techniques, we think it should be taking a broader and deeper perspective by, for example, considering how it can lead wider projects, activities and processes which promote market engagement, development of new markets, and open use of data.
- 1.11 The expectations below are set out as key themes relating to SONI's role as part of the energy transition, and which cut across various aspects of the service activity. We set out behaviours that we would expect from SONI and provide illustrative examples and/or required specific activity to help clarify how these may be met. We set out our exhaustive expectations (which are related to but go further than these energy transition related expectations) and our view of how these may map to various services (to support SONI in designing its service level strategies) as part of the annex: Upfront service expectations, at the end of this annex. We are keen to get stakeholder views on these expectations.

Collaborating and coordinating through a robust, transparent and open approach to data

- 1.12 We consider that SONI should be taking a lead role in whole system development by openly sharing its relevant data and making its TSO actions transparent to enable market participants make efficient operational and investment decisions; and ensure that its systems and processes are kept up to date.
- 1.13 Utility companies are beginning the process of digitalisation whereby they improve the way they use data openly and digital technologies to generate value for third party stakeholders. We request that SONI develops a digitalisation strategy which could be submitted as part of its first full draft forward plan and that it should engage and collaborate with a range of

stakeholders as part developing this (and specifically and clearly document the learnings from this as part of the piece). We would expect this strategy to be updated annually. Some of the aspects that SONI may want to consider and include as part of this are:

- Set out a clear strategic ambition for how digitalisation across different TSO SONI services is going to benefit consumers and the role that SONI is going to play.
- Considering a wide range of best practice and lessons learned elsewhere that could be relevant to open sharing of data and consider what may work in an NI context (both local issues and NI wide level). For example, considering other highly regarded actions from other utilities and policy vehicles (such as the GB energy data taskforce), and wider research and initiatives.
- Understanding of user needs. For example, new data needs and existing data improvement needs (and clear line of sight of how these flow into proposed actions). We also require SONI to set out how it is going to collaborate with and engage with users.
- People planning: how SONI is going to ensure that its workforce is going to have the right capabilities in areas such as digital, data and technology. This could include but is not limited to upskilling, recruiting skills, diversity and how these will be specifically embedded into its business operating model.
- Governance and corporate interactions and accountability. For example, how exactly senior ownership, accountability and SONI board-level will take responsibility for delivery of the digitalisation strategy and action plan will work.
- How SONI is going to coordinate activities with other organisations, including but not limited to NIE Networks.
- Actions and delivery to meet users' needs across the services that SONI offers: cost, benefit, options (including those that give 3rd parties *direct* access to data), validation, prioritisation and how exactly they will lead to the performance framework outcomes. Each planned activity should be demonstrably aligned to and driven by user and stakeholder needs.
- In keeping with themes of our regulatory approach, we expect SONI to take a service based approach. SONI should set out clearly whether and how its work in bullets 3 to 7 is relevant according to different services depending on where most value can be gained for

consumers. This element could be included within its individual service level strategies.

- 1.14 In gathering and providing data to the market we consider that SONI's data should be user-friendly. To support this SONI should be engaging effectively with market participants to understand their needs, for example, in terms of content, format and frequency. SECG was also concerned about clarity around the actions SONI takes which may influence whole system costs. For example, how specifically its actions influence dispatch balancing costs. We, therefore, also consider that SONI's data should be comprehensive: gathering as much information as necessary, disclosing information on system and its actions (where safe and reasonable), and ensuring its processes can effectively allow stakeholders to propose changes to the information it shares or publishes transparently, and that it provides sufficient clarity on reasons for withholding information. We consider that SONI should maintain up to date robust IT systems and seek to continuously improve its information. This should be so that information is accurate and unbiased.⁵³ For example, we consider this could be information relating to demand and wind forecasts and balancing costs.

Developing markets through competition and stakeholder engagement and collaboration

- 1.15 The way SONI designs and procures system services and its approach to dispatch and scheduling can affect providers' ability to compete and revenue available, and affect price signals and cost in wholesale market. SONI should be ensuring the rules and processes for procuring system services (and/or dispatch and scheduling) maximise competition, where possible, and are fair and transparent.
- 1.16 In terms of competitiveness, we encourage SONI to continue to move to more market based approaches. For example, it could consider and develop commercial framework tenders or make more use of auctions, and transparently consider whether the market may be better placed to provide certain system service. Where it cannot take a more market based approach, SONI should transparently and robustly justify why it is not in the interest of consumers to do so and set out how it may support development of a market.
- 1.17 In terms of fairness, we would expect SONI to design and procure system services and design control centre tools in a way which facilitates existing and new providers to compete on a level playing irrespective of size or type.

⁵³ By accurate we mean that information is correct at the time of publication and as close as reasonably possible to the actual value. By unbiased we mean that information is not skewed in any way and is as accurate/close as reasonably possible to its true value.

SECG had concerns that this could include, for example, ensuring a technology neutral approach to procurement of system services. SECG also had concerns that SONI should ensure that its service and technical requirements for system services and design of dispatch and scheduling tools and processes remain responsive to changing technologies and innovation and do not unduly restrict access to certain market participants. For example, SONI may want to ensure that there is an effective public process that ensures that its system service technical requirements are regularly reviewed by allowing stakeholders to collaborate with SONI and input effectively into their design. We also consider that SONI should be transparent: for example, in communicating and justifying its procurement need.

- 1.18 SONI should be actively partnering and collaborating with industry in preparing and implementing future programmes of work where it can. For example, it may want to seek a balance of proactively seeking out partners to adopt trial based approaches with partners and other organisations (across the electricity value chain and potentially beyond), as well as using more traditional desk based planning exercises.

Collaboration and coordination with NIE Networks (and other 3rd parties) across its various roles as a TO, DNO and DSO

- 1.19 SONI should be taking a whole system approach by working across system boundaries with NIE Networks and other 3rd parties.
- 1.20 We consider that SONI should be participating in and driving forward industry processes, across its system operation and adequacy and network development and system planning roles in particular.
- 1.21 We consider that SONI should be engaging with stakeholders to understand the long terms needs of the system and ensure that its processes remain fit for purpose by being responsive to reasonable needs of customers. For example, we understand that SECG seeks clarity on how SONI assesses system needs, and so we consider that SONI should set out clearly for stakeholders its processes and methodologies for forecasting and assessing system needs, including effective opportunities for these to be tested with / challenged by market participants and other stakeholders.
- 1.22 SONI should be working with NIE Networks and other stakeholders to ensure that its TSO roles and responsibilities are clearly defined and unnecessary overlap and duplication is removed or minimised with respect to the roles NIE Networks undertakes as a TO, DNO and DSO. For example, with respect to the DSO and TSO interaction, SONI may want to develop a whole system strategy, involving NIE Network, via public process, aimed at developing sharing recommendations on common principles and criteria with

respect to its TSO role in data management and information exchanges with NIE Networks (with resulting in innovative and value for money proposed deliverables and actions to take a whole systems approach in line our regulatory guidance including with reference to paragraph 3.12 to 3.13 below). More generally, we expect it to work with NIE Networks to update the Transmission Interface Agreement (TIA) as swiftly as possible where and when relevant.

- 1.23 SONI should collaborate, communicate and coordinate with NIE Networks to build a common understanding of whole system requirements and where actions taken by one system/network operator could have cross-network whole system impacts, and then identify and swiftly implement actions that benefit the whole electricity system and that optimise synergies using resources optimally across the network. For example, with respect to its role in network development and system planning, SONI should be developing non-network options which may reduce the need for network reinforcement and work with NIE Networks to develop solutions at distribution network level that relieve transmission network challenges and vice versa. We consider that SONI should, where relevant, deliver its actions appropriately and as swiftly as possible.
- 1.24 SONI will need to collaborate closely, meaningfully but proportionately with NIE Networks to inform, develop and implement its actions. For example, gathering and sharing information efficiently (for example, possibly by developing sharing protocols or other coordination processes with each other) and co-developing whole system approaches for assessment (for example, by developing common and transparent approaches to modelling).