

SONI TSO Price Control 2020 – 25

SONI Response to the UR Licence Modifications Consultation

22 October 2021



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1 Executive Summary

Introduction

- 1.1 SONI welcomes this consultation on the modifications to our licence that are necessary to implement our price control from 2020 to 2025. While we welcome many aspects of the new price control framework, we have specific concerns about aspects of the modifications proposed and the process followed to date. These are set out in our response.
- 1.2 We acknowledge the substantial amount of work that has gone into this overhaul of SONI's revenue arrangements to update them for a new decade. This process has been ongoing for three years and has introduced a fresh approach. This formal consultation response is by necessity focused solely on the issues that remain to be resolved, however it should be read in the context of the substantial transformation that the UR team has delivered.
- 1.3 Actions over this period will set the direction for the further decarbonisation of the energy system in Northern Ireland and it is vital that SONI is able to play its part in that transition. Our response is focused on ensuring that the funding provided to SONI through this update to its licence provides a sustainable foundation for the delivery of the new renewable energy targets while ensuring ongoing compliance with the evolving legal framework in which we operate.
- 1.4 We therefore remain very keen to work collaboratively with the UR to resolve these remaining issues to ensure that we can focus on delivering the new energy strategy for the benefit of all in Northern Ireland.

Key Issues

- 1.5 In this response, SONI sets out twelve key issues that it has identified across the proposed modifications and process followed to date. We present these in four groupings, which we hope will facilitate meaningful engagement around our concerns and the remedies necessary for each set. We begin by identifying incorrect references within the Article 14 notice, then highlight errors that have a material commercial impact on SONI, we then set out the main errors in the process to date, and finally we highlight areas with a lack of clarity with the Final Determination and Licence Modifications.

Statutory Notice

- 1.6 The statutory processes around the modification of SONI's licences are set out in Article 14 of the Electricity (Northern Ireland) Order 1992. The notice issued by the UR appears to SONI to contain errors and falls short of the standard expected under the Northern Ireland regulatory framework.

Table 1.1 Errors in Article 14 Notice

Key Issue	Description	SONI Response
<p>Article 14 Notice Validity</p>	<p>The notice refers to an irrelevant section of the Electricity (NI) Order 1992. (Article 8.1 relates to Prohibition on unlicensed supply, etc.) and omits the correct legislation.</p> <p>In addition, the drafting of the Article 14 notice attempts to give full effect to the Final Determination, which is contrary to the UK regulatory framework which is based on regulatory decisions being codified in licences.</p>	<p>SONI considers this notice to be invalid because it refers to legislation that is irrelevant to this process.</p> <p>Furthermore, the UR has not properly codified its decisions into the Licence. This is considered substandard as the Article 14(2) Notice and the accompanying modifications should provide a clear articulation of the obligations imposed on SONI.</p> <p>SONI considers that the UR will need to undertake a further Article 14 notice which includes the correct references to the appropriate legislation.</p>

Commercial Impact

1.7 In its approach paper, the UR states that “the price control framework for SONI should represent a financeable package, which covers reasonable remuneration for the costs and risks which SONI bears¹”. When assessing these draft modifications, SONI has identified three areas where the proposals fall materially short of this stated aim. These are summarised in the table below, with supporting material included within our main response.

¹ [Approach Paper](#), Page 10

Key Issue	Description	SONI Response
<p>ENTSOE membership & CORESO Allowances</p>	<p>The UR changed the categorisation of these costs, increasing the risk to SONI between Draft and Final Determination without consultation, and in turn, resulting in a material cost exposure for SONI under the new mechanism for fees which are outside the control of the TSO.</p> <p>The Final Determination includes a provision for these costs in the base allowances and they are subject to the 75/25 risk share mechanism. This provision is expected to be at least £2 million short over the 5 years due to increased scope and cost reallocations due to Brexit.</p> <p>The Licence modification and the associated notice ignores text in Appendix A to Annex 5 of the Final Determination which states specifically for these cost areas that SONI can seek additional funding '<i>in the event of material cost increases</i>'.</p>	<p>Based on recent cost estimates from ENTSOE and CORESO, SONI estimates that its contribution to the increased fees will be in excess of £500k over the price control period (based on the application of the 75/25 risk share arrangements).</p> <p>SONI therefore considers that there are errors on a number of fronts:</p> <ul style="list-style-type: none"> • Failure to comply with the EU Network Codes which provide SONI with the right to recover efficiently incurred costs associated with these activities • Failure to provide regulatory certainty by exposing SONI to uncontrollable risks and costs exposure • Failure to achieve stated objectives • Failure to account for the roles and responsibilities of SONI • Acted ultra vires by failing to consult on the change of approach on ENTSOE membership and CORESO allowances <p>SONI is requesting that the licence modifications include a clause to ensure these costs are fully recoverable.</p>

Key Issue	Description	SONI Response
<p>Delays in Price Control Process</p>	<p>The Price Control start date was October 2020.</p> <p>The UR published a timetable in the Final Determination stating that the price control process would be completed in April 2021.</p> <p>Based on the current status of licence modifications it is now expected that the process will not be completed until 2022.</p> <p>The scale of the delay is limiting SONI's ability to implement the price control fully and leaves SONI without certainty around its ability to retain revenues received through tariffs since 1 Oct 2020, in addition to other notable risks.</p>	<p>SONI has identified three direct impacts of the delay in the price control process:</p> <ol style="list-style-type: none"> 1) The asymmetric risk proposal is significantly undervalued, as SONI cannot avail of the new uncertainty mechanisms. Therefore, the value of the asymmetric risk premium for Years 1 & 2 should be recalculated to reflect the additional risk imposed on SONI. 2) As the conditional cost sharing guidance associated with the price control is not yet published, the calculations cannot apply to year 1 of the price control. 3) The Evaluative Performance Framework was due to apply from year 3 of the price control following the completion of a transition year. SONI agrees that the transition year is a key aspect of this framework and requests that the incentive arrangements are deferred by 1 year to allow a transition year to be progressed. <p>SONI is requesting that the licence modifications are adjusted to reflect the impact of the delay in completing the price control process</p>

Key Issue	Description	SONI Response
<p>Hard Coded and Understated Value for Asymmetric Risk Premium</p>	<p>The UR set a value for the Asymmetric Risk Premium (in line with the approach used by the CMA)</p> <p>However, SONI considers that the UR understated the forecast of costs that are applicable to the Asymmetric Risk Premium.</p>	<p>SONI has provided what we consider to be the quantum of revenue where we are exposed to asymmetric risk over this price control, which should be reflected in the Asymmetric Risk Premium (ARAt) term to ensure that the price control remains consistent with the 2017 CMA determination.</p> <p>This reflects:</p> <ul style="list-style-type: none"> • The impact of the delay in Years 1 & 2 • Rectification of an error in the UR calculations • Correction of the treatment of ENTSO-E & CORESO costs • Recognition of the expected significant expenditure required on Electricity Balancing Guideline (EBGL) which the UR did not consider in its estimates. <p>SONI is requesting that the licence modifications are adjusted to reflect the value of the ARAt term from £136k per year to £225k per year.</p>

Price Control Process

1.8 SONI has sought to work with the UR over the past three years to ensure that a robust process was followed for the delivery of this Price Control. Despite the considerable resources that SONI has applied to this exercise, and the additional time taken by the UR to reach this stage, we have identified four aspects of the process that undermine this consultation exercise and, further impact the implementation of the Price Control itself. These shortcomings are outlined below, and expanded upon further in our detailed submission.

Key Issue	Description	SONI Response
<p>Unpublished Guidance Documents</p>	<p>SONI notes that the three guidance documents referenced in the licence modifications and Article 14 notice have not been published. These are:</p> <ul style="list-style-type: none"> • Requirements and Guidance on Conditional Cost Sharing; • Requirements and Guidance on the Evaluative Performance Framework; and • Requirements and Guidance on Uncertainty Mechanisms. <p>The UR is therefore requesting stakeholders to comment on modifications without the opportunity to consider all the relevant information.</p> <p>We note that the recent draft versions of the guidance documents provided to SONI contains significant changes to the versions in the public domain (published in Dec 2020 for consultation) and have not been made available to other parties who may wish to respond to this Article 14 notice.</p>	<p>SONI considers this as an error in process for three key reasons:</p> <ul style="list-style-type: none"> • Failure to achieve stated objectives by not finalising a considerable amount of guidance material (which is meant to drive the application of the requisite provisions of the price control). • To rely upon unpublished and non-consulted (but updated) guidance documents and definitions to give effect to these modifications is ultra vires. • The UR has introduced modifications which bypass The Gas and Electricity Licence Modification and Appeals Regulations (Northern Ireland) 2015 – as SONI has been denied an appropriate appeal route to decisions that will have a material impact on its operations. <p>SONI considers that the UR will need to undertake a further Article 14 notice which includes the published final guidance documentation.</p>
<p>References to ‘Price Control Decision Paper’</p>	<p>The Licence Modifications contain 17 references back to the ‘Price Control Decision Paper’</p> <p>This is a move away from UK regulatory practice whereby the decisions made by a regulator are fully codified in the licences.</p>	<p>SONI considers this as a failure to provide regulatory certainty and a departure from UK regulatory practice.</p> <p>The approach proposed by the UR is flawed considering that the Final Determination includes references to:</p> <ul style="list-style-type: none"> • consultation documents that have not yet been finalised; • deliverables which are not defined; and • dates that have already passed. <p>SONI is requesting that all references to the ‘Price Control Decision Paper’ be removed from the licence.</p>

Key Issue	Description	SONI Response
<p>Proposed Allowance Adjustments due to under delivery</p>	<p>The Final Determination states that the UR may adjust SONI's allowances for non/partial delivery of deliverables.</p> <p>The processes for making any adjustments are not defined.</p>	<p>SONI's considers that the UR approach is erroneous due to two reasons:</p> <ul style="list-style-type: none"> • A failure by the UR to provide the guidance and definitions necessary to assess whether the objective has been achieved; and • A failure to detail the effect of the licence modifications for this proposed adjustment. <p>SONI is requesting that the UR provides additional clarity on any adjustments they plan to undertake. SONI has offered to support the UR in this area.</p>
<p>Lack of definition of Deliverables</p>	<p>The deliverables spreadsheet is published in draft form.</p>	<p>SONI's considers that the UR approach is erroneous due to two reasons:</p> <ul style="list-style-type: none"> • A failure by the UR to provide the definitions necessary to assess whether the objective has been achieved; and • A failure to detail the effect of the licence modifications for this proposed adjustment. <p>SONI is requesting that the UR provides additional clarity on the definition of deliverables. SONI has offered to support the UR in this area.</p>

Lack of Clarity in Final Determination and Licence Modifications

1.9 SONI acknowledges the considerable work that has gone into developing the suite of documentation required for a price control of this complexity. However, there are four areas where we are concerned that there is a lack of clarity across the Licence Modifications and Final Determination which introduce ambiguity to the operation of the control. As set out in the table below and expanded upon in our submission, these place inappropriate risk onto SONI that is not reflected within the package as a whole.

Key Issue	Description	SONI Response
<p>Introduction of term “Manifestly Unreasonable”</p>	<p>The UR has introduced the term ‘Manifestly Unreasonable’ which allows the UR to exclude actual costs if they deem the costs meet this undefined term.</p> <p>SONI notes that significant work was undertaken to introduce the Demonstrably Inefficient or Wasteful Expenditure (DIWE) term in the licence. This includes detailed guidance documentation.</p> <p>The introduction of the “Manifestly Unreasonable” term creates uncertainty as to when it will be used rather than DIWE</p> <p>This concept was not consulted on as part of the work on the price control design.</p>	<p>SONI has demonstrated, via a worked example, that the DIWE term will suffice for any scenario thereby deeming the introduction of “Manifestly Unreasonable” unnecessary.</p> <p>SONI is requesting that this term is removed from the licence in its entirety.</p>
<p>Removal of Dispatch Balancing Costs incentive</p>	<p>The UR has removed the Dispatch Balancing Costs incentive formulae and associated definitions from the licence, describing the incentive as ‘no longer required’.</p> <p>This was not referenced as part of the work on the price control design.</p>	<p>SONI considers this incorrect as this incentive is a SEM Matter. The UR would be acting ultra vires by removing this term and the associated definitions because their removal should be as a result of a SEMC decision. The SEM Committee has not yet consulted upon this matter.</p> <p>SONI has a letter stating that the incentive arrangements remain under review. Therefore, the removal of the licence formulae and definitions is premature.</p> <p>The deletions also cause other licence conditions to be rendered incomplete (condition 39).</p> <p>SONI is requesting the UR to reinstate this incentive and the associated definitions.</p>

Key Issue	Description	SONI Response
Selection of Uncertainty Mechanism for Additional Approved Costs	<p>The UR has given itself the unilateral ability to change the uncertainty mechanism used in its approvals.</p> <p>This may result in the risk profile used by SONI when preparing its submission to be inappropriate for the mechanism eventually selected by the UR and therefore not fully considered in the UR decisions</p>	<p>SONI is requesting clarity in the use of these mechanisms.</p>
AOt Definition – Actual Operating Expenditure and AC_Rt Definition	<p>The UR has included wording that does not allow SONI to recover all of our actual costs associated with our full suite of duties.</p> <p>The drafting limits cost recovery to <i>‘expenditure is incurred in the performance of its activities that are authorised by or subject to obligations under the Licence’</i></p> <p>However, many of legal obligations that apply to SONI are not specifically defined in the licence. Therefore, the current drafting is too restrictive and would result in SONI being unable to recover legitimate costs in the Revenue Entitlement calculations.</p>	<p>SONI considers that this issue is easily addressed by including additional drafting that reflects the full remit of SONI's obligations.</p> <p>SONI has proposed alternative drafting to address this concern.</p>

Drafting of the Annex

1.10 In addition to setting out its key concerns around the substance of the proposed modifications and the process followed to reach these erroneous conclusions, SONI also provides detailed comments on the updated licence text and formulae, along with proposed alternative drafting where relevant.

Price Control Timelines

1.11 While we set out the specific commercial impact of the delays to the 2020-25 price control within the key points above, we would also highlight our dissatisfaction around what we see as a continuing trend. Since 2010, SONI has entered a tariff year with a codified revenue entitlement on five occasions, leaving seven years with revenue uncertainty. This regulatory

instability and risk is compounded by delays to approvals under the uncertainty mechanisms, with the UR on occasion taking longer than the timeframe of four months set out in the CMA order.

- 1.12 While we do not focus on the cumulative impact of these sustained periods without funding certainty within this response, we would greatly welcome assurance from the UR that future price controls will be codified before the start of the period and that uncertainty mechanism decisions will be provided within the specified timeframe.

Next Steps

- 1.13 SONI notes that due to the invalidity of its consultation the UR will need to undertake a further Article 14 notice consultation. SONI would welcome early engagement with UR on the substance of this response. We consider that the concerns we have raised can be addressed through updated drafting of the licence modifications and guidance documentation. SONI is available to support the UR in these activities and where appropriate we have proposed alternative drafting in our response. Ultimately, SONI wishes to work with the UR to ensure that a sustainable outcome to this process is achieved, which will allow us to focus on delivering value for consumers in Northern Ireland.
- 1.14 In parallel, we will be progressing requests via the existing uncertainty mechanism to address the shortfall in funding for vital initiatives that will ensure the ongoing operation of the grid and markets and support the decarbonisation of Northern Ireland's energy supply.

2 Introduction

- 2.1 Actions over the period covered by this price control will set the direction for the further decarbonisation of the energy system in Northern Ireland and it is vital that SONI is able to play its part in that transition. Our response to this consultation is focused on ensuring that the funding provided to SONI through this update to its licence provides a sustainable foundation for the delivery of the new renewable energy targets, while ensuring ongoing compliance with the evolving legal framework in which we operate.
- 2.2 We acknowledge the substantial amount of work that has gone into this overhaul of SONI's revenue arrangements to update them for a new decade. This process has been ongoing for three years and has introduced a fresh approach. This formal consultation response is by necessity focused solely on the issues that remain to be resolved, however it should be read in the context of the substantial transformation that the UR team has delivered.
- 2.3 In this paper, SONI has provided a comprehensive response to the proposed modifications to our Licence to Participate in Transmission. We highlight a number of substantial issues that we consider fundamental to SONI's revenue and the delivery of the objectives that the UR set out to achieve through this price control process.
- 2.4 Throughout this price control process, SONI has prioritised engagement with UR and has sought to provide as detailed information as was available to it at the time. While some delays to the process were inevitable because it took place in parallel with the development of decarbonisation strategies and a global pandemic, the nine month gap between the publication of the Final Determination on 21 December 2020 and the Proposed Licence Mods on 24 September 2021 was not signalled to stakeholders and is contrary to regulatory best practice. We have raised our significant concerns on the protracted process that SONI has been subjected to later in this paper.
- 2.5 It is worth noting however that in parallel with the price control process, SONI has continued to proactively progress initiatives such as the MIP Solver project, 'Shaping our Electricity Future' consultation, preparations for the Moyle upgrade project and supporting the high level design of the new arrangements for the procurement of System Services to ensure that the protracted process has a minimal effect on consumers.
- 2.6 SONI acknowledges receipt of a draft version of the licence modifications in late June 2021 and the engagement that followed over the summer months. However, we note that the majority of comments and concerns we fed back to the UR have not been considered or addressed in the published version of the licence modifications. We have therefore repeated many of the points previously raised through our earlier engagement.
- 2.7 We note that the UR is currently progressing a consultation on changes to SONI's governance arrangements in parallel to this price control process. We note that this consultation is taking place before the outcome of that parallel process is known. Therefore, this response is presented in the context of our current governance arrangements and the stated effect of the modifications as set out by UR can also only be construed and considered in that context.

2.8 As indicated in the Final Determination (Paras 1.15 – 1.17), we expect that depending on the UR's determination in relation to SONI governance, publication of a separate and specific Article 14 notice will be required including a reopening of the specific modifications here currently proposed. We will of course respond to any modifications that may follow from the governance review at the appropriate time.

2.9 We have structured our response under the following headings:

- Introduction
- Key Issues
- SONI Concerns relating to Licence Modifications

2.10 SONI would welcome early engagement with UR on the substance of this response. We consider that the concerns we have raised can be addressed through updated drafting of the licence modifications and guidance documentation. SONI is available to support the UR in these activities and where appropriate we have proposed alternative drafting in our response. Ultimately, SONI wishes to work with the UR to ensure that a sustainable outcome to this process is achieved, which will allow us to put all of our focus onto delivering value for consumers in Northern Ireland.

2.11 SONI remains keen to progress the important work required to facilitate achievement of the new decarbonisation targets for Northern Ireland. The finalisation of these Licence modifications which introduce new frameworks for risk sharing and performance incentives, is a key enabler of that process. We therefore welcome the publication of this consultation and commit to working with the UR to bring this process to a close.

3 Key Issues

3.1 SONI has carefully reviewed the proposed modifications and in this response sets out twelve key issues that we have identified across the proposed modifications and process followed to date. We present these in four groupings, which we hope will facilitate meaningful engagement around our concerns and the remedies necessary for each set. We begin by identifying incorrect references within the Article 14 notice, then highlight errors that have a material commercial impact on SONI. We then set out the main errors in the process to date, and finally we highlight areas with a lack of clarity with the Final Determination and Licence Modifications.

Statutory Process

Key Issue 1: Validity of the Notice pursuant to Article 14(2) of the Electricity (Northern Ireland) Order 1992

- 3.2 The statutory processes around the modification of SONI's licences are set out in Article 14 of the Electricity (Northern Ireland) Order 1992. The notice issued by the UR appears to SONI to contain errors and falls short of the standard expected under the Northern Ireland regulatory framework.
- 3.3 The notice refers to an irrelevant section of the Electricity (NI) Order 1992. (Article 8.1 relates to Prohibition on unlicensed supply, etc.) and omits the correct legislation.
- 3.4 SONI considers that the Article 14 Notice published by the UR on 24 September 2021 to be invalid because it refers to legislation that is irrelevant to this process.
- 3.5 Furthermore, SONI notes the inclusion of the following paragraph in the Article 14 Notice appended to the Consultation paper:
- 'The Final Determination provides a full statement of both the effects of the proposed modifications and the reasons for them, and should be treated as incorporated into this notice by reference. The Authority considers that the decisions made in the final determination, as embodied in the modifications, will ensure compliance with its duties at Article 12 of the Energy (Northern Ireland) Order 2003 during the period of the 2020-2025 price control'.*
- 3.6 SONI is very concerned about the inclusion of this wording as it implies that the obligation to codify the price control decisions into the licence is being bypassed. This in itself is considered substandard, as the Article 14(2) Notice and the accompanying modifications should provide a clear articulation of the obligations imposed on SONI. Instead this reference leaves ambiguity.
- 3.7 As a result of both of these concerns, SONI considers that the Article 14 notice is not valid.

SONI Position

- 3.8 The errors identified undermine the legal integrity of the process undertaken by the UR. This Price Control will bind SONI for five years and therefore, we are keen to ensure it is legally sound. As such, SONI is committed to working with the UR in resolving the issues related to the Notice. The sanitisation of this process will require a new Article 14 Notice and consultation to be initiated.

Commercial Impact

- 3.9 The UR approach paper states that “the price control framework for SONI should represent a financeable package, which covers reasonable remuneration for the costs and risks which SONI bears.” When assessing these draft modifications, SONI has identified three areas where the proposals fall materially short of this stated aim. These are expanded upon below.

Key Issue 2: ENTSOE membership & CORESO Allowances

- 3.10 SONI strongly objects to the removal of the right to recover ENTSO-E and CORESO membership costs via the Dt mechanism in paragraph 8.1. Until the publication of the Final Determination in December 2020, SONI’s understanding was that it would be able to claim 100% of any efficiently incurred overspends via the conditional cost sharing mechanism². We had therefore assumed that there was no risk of any over or under-recovery of the costs of our membership of ENTSO-E or CORESO given that we have very little control over:
- our status as a member;
 - the scope of work undertaken by ENTSO-E and CORESO; and
 - the cost of that work.
- 3.11 The future trend of these obligations was extremely uncertain until the terms of the UK departure from the EU was confirmed in late 2020. Had the UK government decided to leave without an agreement, it is highly probably that SONI would have had to resign from its membership of ENTSO-E and future cooperation with EU TSOs through CORESO would have been unlikely.
- 3.12 In addition to the categorisation of costs in Figure 8 of the Draft Determination, the UR provided SONI with clear assurances³ that the baseline would be uplifted for efficient increases in costs:

“It is possible in practice for there to be an over-spend in one area and an underspend in another. In such cases, we would first look at the evidence that higher costs have been incurred in one area due to the efficient costs of justified improvement in performance, and if so this would effectively imply an uplift to the

² This was the approach consulted on in the Draft Determination

³ see paragraph 6.65 of Appendix A to Annex 5 of the Draft Determination

ex-ante baseline, from which the appropriate treatment of any under-spend against that uplifted baseline could then be assessed. This would enable a financial upside (reward) to SONI even if the overall spend was more than the baseline.”

- 3.13 This underpinned our response to that consultation and consequently SONI did not raise any specific concerns about the change in treatment because cost recovery appeared to be secure. Conversely there did not appear to be any possibility that SONI could have obtained a windfall (in relation to allowances for membership fees) if political circumstances meant that it was no longer able to be a member of these organisations.
- 3.14 The approach proposed by the UR in its Draft Determination was that all costs under the price control (except System Services, TNPP work, TUoS and CAIRt) would be subject to the conditional cost sharing mechanism (see Figure 8 of the Draft Determination). However, in the Final Determination, the UR changed this position and altered the mechanism such that a subset of costs would sit outside the Conditional Cost Sharing arrangements as well as the introduction of a threshold before the conditional cost sharing arrangements apply. The principle set out in Paragraph 6.65 of Appendix A to Annex 5 of the Draft Determination therefore no longer applied.
- 3.15 The impact of these changes is such that the cost for ENTSO-E and CORESO membership now sits outside the conditional cost sharing arrangements and are subject to a mechanistic cost sharing arrangement. We note that this is not clearly stated in the Final Determination (see our comments in section 4.7 in relation to Table A of Annex 1). This means that 25% of any overspend against the allowances will need to be funded by SONI. Considering both the unpredictable and uncontrollable nature of these costs and the fact that SONI has a legal obligation to retain membership, SONI deems this decision as incorrect.
- 3.16 SONI considers that this is an unintended consequence of the multiple changes made by the UR between its draft and final determination. As highlighted above, if the Brexit decisions had been different, this allowance would be a windfall for SONI, which we do not consider is in the interest of customers. SONI considers that the UR did not fully test the impact of the changes made between its Draft and Final Determination. This has resulted in a material exposure for SONI as discussed below. By making such a significant policy change in the Final Determination and one which will have a substantial financial impact on SONI, the Utility Regulator has denied us and any other stakeholder the opportunity to consider and comment on these issues.
- 3.17 It is only in recent months that SONI’s future position in ENTSO-E and CORESO has been confirmed, while National Grid has had to resign from ENTSO-E and reduce its shareholding in CORESO. During this consultation period, SONI has been informed of an estimated increase in our ENTSO-E annual membership fee from less than £100k to approximately £350k per annum to reflect the post Brexit arrangements. This may increase further as the full outworking of National Grid’s resignation emerges. The provision included in the price control baseline is £75k per annum, or £350k over the five years.
- 3.18 The services to be provided by CORESO are mandated by the Network Codes and regulatory approved methodologies. The UR included a provision of £135k per year for these costs. In January 2021, the UR approved SONI’s recovery of its actual membership

fee for 2019/20 of £161k (in April 2014), a price which is notably higher than the price control provision.

- 3.19 The costs of the services to be provided over the remainder of the price control are still being developed, however the uplift to cover the provision of new services is expected to be measured in the hundreds of thousands of pounds.
- 3.20 As set out in Table 3.1 below, when these factors are combined, the UR's proposed price control package would leave SONI contributing more than half a million pounds towards these mandatory fees.

Table 3.1: ENTSO-E and CORESO Fees 2020-25

£k	2020-21	2021-22	2022-23	2023-24	2024-25
Allowances for ENTSO-E and CORESO membership ⁴	210	210	210	210	210
Estimated costs for ENTSO-E membership ⁵	95k	C. 350k	C. 350k	C. 350k	C. 350k
Estimated costs for CORESO membership ⁶	210k	>£400k	>£400k	>£400k	>£400k
Total membership costs	305	>£750k	>£750k	>£750k	>£750k
Shortfall	95	>540	>540	>540	>540
SONI Exposure⁷ to uncontrollable costs (25%)	24	>135	>135	>135	>135
Total SONI Exposure	>564				

- 3.21 This proposed approach also appears to contradict the relevant Network Codes, which all contain an obligation on the UR to allow recovery of the efficiently incurred costs of these activities. This obligation on the UR further calls into question the recent UR decisions of (15 July 2020 and 16 April 2021) where it refused to provide funding for SONI's

⁴ This is based on the allowances included in the Final Determination.

⁵ Estimate for ENTSO-E membership costs based on current estimate for 2022 and does not reflect the full impact of NGESO's resignation, therefore costs may be higher in future years

⁶ The CORESO budget process is ongoing. The quantum of the increase to reflect the new services is still being calculated but is expected to increase SONI's costs by several hundred thousand pounds

⁷ This is the lowest amount that SONI would contribute. If efficiencies are found elsewhere, they would reduce the share paid for by customers under the current proposals, contradicting Paragraph 6.65 of the Appendix to Annex 5 of the Draft Determination.

membership of CORESO and ENTSO-E via the Dt uncertainty mechanism, despite this being contrary to the licence as currently extant.

3.22 The Final Determination contains the following narrative⁸ specifically relating to licence fees, ENTSO-E and CORESO costs:

‘This is subject to clarification that SONI will be able to make a submission for additional allowances under the Dt uncertainty mechanism in the event of material cost increases. We will consider any such submission on its merits and in line with any applicable regulatory guidance. Any such submission would need to exceed the materiality threshold.’

3.23 It is therefore clear that it is the UR’s intention that SONI can recover material cost increases associated with licence fees, ENTSO-E and CORESO costs via the Dt uncertainty mechanism. The drafting in the proposed licence modifications does not reflect this position and indeed the references to the ENTSO-E membership costs in paragraph 8.1 have been deleted.

3.24 We therefore request that the right to recover full costs that we incur efficiently (in line with European legislation) as a result of our mandated membership of ENTSO-E and CORESO via the Dt uncertainty mechanism is detailed in the Licence. In addition, we request that the UR rescinds its decisions of 15 July 2020 and 16 April 2021 because:

- the UR is obliged to facilitate SONI’s recovery of these costs under EU law which continues to apply in Northern Ireland following the UK departure from the EU;
- the position of the all island electricity market is enshrined in the Trade and Cooperation Agreement (**TCA**) and NI Protocol. No action should be taken which could result in the UR and as a consequence, SONI, breaching the obligations flowing from this legislation;
- the unavoidable increase in these costs if SONI was to remain a member of these organisations was not fully considered in the UR’s Draft or Final Determination
- different sections of the Final Determination are contradictory. The allowances have been included under the mechanistic cost sharing mechanism, however a provision to allow SONI to recover these costs, if there are material cost increases, is also stated.
- it seems unintentional that the UR would have created a situation where SONI may have been able to retain a windfall had it be forced to resign from these organisations for external political reasons, therefore symmetrical treatment should be afforded; and
- the UR made a significant change to the treatment of these costs between draft and final determination and the risks to SONI were not set out in the UR’s consultation on its Draft Determination, therefore SONI was not provided with an opportunity to make representation on it or to highlight the major concerns the proposed approach creates.

⁸ See Annex 3 paragraph 4.75

SONI Position

- 3.25 SONI considers this as a material issue. Furthermore, the current drafting is erroneous due to the following reasons:
- Failure to provide regulatory certainty and expose SONI to risks and costs exposure
 - Failure to achieve stated objectives
 - Failure to account for the roles and responsibilities of SONI
 - Acted ultra vires by failing to consult on the change of approach on ENTSO-E membership and CORESO) allowances
- 3.26 SONI considers that further drafting is needed to properly reflect the UR's intentions as specified in the Final Determination into the Licence (along with the necessitated consultation). SONI's expectation is that all mandated European related costs should be full recoverable, considering under the current political landscape they are both unpredictable and uncontrollable. A de minimis threshold should not apply as the UR is legally obligated to ensure the TSO can recover all efficiently incurred costs.
- 3.27 SONI requests that the UR includes the necessary drafting in the licence modifications to fully reflect its intended treatment thus providing SONI with absolute certainty of full cost recovery for these mandatory activities and to address the material concerns detail above.

Key Issue 3: Delays in Price Control Process

- 3.28 The Price Control start date was October 2020. The UR published a timetable in the Final Determination stating that the price control process would be completed in April 2021. However, based on the current status of licence modifications SONI estimates that the process will not be completed until 2022.
- 3.29 SONI has identified three direct impacts of the delay in the price control process which we discuss below.
- 3.30 In the Final Determination, the UR made reference to the delays in the price control process⁹ highlighting both the impact of the submission of the SONI Business Plan and Covid 19 for the delays. SONI understands both these delays. SONI welcomed the clear timelines detailed in the Final Determination (Table 3) which, if adhered to, would have resulted in the price control fully being implemented seven months after the start date of the price control period. Whilst this delay would not have been ideal, SONI concluded it could manage the uncertainty for this time period. Indeed, the timing was such that SONI's revenue and risk position would have been known and understood before the annual tariffs were set for the second year of the price control.
- 3.31 Since the Final Determination was published, SONI has been engaging regularly with the UR to understand the remaining timeframes for the price control process. The UR has been

⁹ Paragraph 1.9

reluctant to provide specific dates or provide any certainty on its timetable. SONI wrote formally to the UR in May 2021¹⁰ to '*urge the UR to please provide certainty on the timeframe for the licence modifications and provide definitive dates for when the licence modifications will be provided to SONI*'. No response was received from the UR.

- 3.32 The delays imposed on SONI have had direct implications on the price control implementation. SONI notes that the UR will have to progress the publication of the guidance documents. The failure to provide the guidance documents alongside the Final Determination denies SONI and all stakeholders the opportunity to ascertain the effects of the licence mods. There is a lack of a timetable available for the completion of these activities. SONI is therefore in the position where year 1 and the vast majority of year 2 of the price control period will be completed without certainty in terms of revenue and therefore increased risk.
- 3.33 SONI has detailed below the key impacts on the price control implementation which are directly impacted by the UR delays, and hence the exposures now facing SONI. We have also set out the actions we consider the UR should take to address our concerns.

Key Issue 3.1: Limited ability to use the uncertainty mechanisms and impact on Asymmetric Risk allowance

- 3.34 The UR has introduced two new uncertainty mechanism terms for the 2020-25 price control (Et and Vt). The delays in completing the price control process means that SONI cannot currently use either of these new mechanisms. Therefore, the intended incentive arrangements cannot be availed of during Year 1 and most of Year 2 which is to the detriment of customers.
- 3.35 During this prolonged delay period, SONI has no option but to progress funding requests via the existing Uncertainty Mechanisms (Dt and Zt). These mechanisms include asymmetric risk which is not accounted for under the Final Determination. Had SONI been aware of the significant delay, we would have signalled this risk to the UR and requested that this is compensated via the calculation of the ARAt term in the licence.
- 3.36 We therefore consider that the UR needs to revisit the calculation of the ARAt terms and reflect the cost of the additional risks that SONI is currently facing in the revenue entitlement. SONI has detailed the projects that it has or plans to progress in years 1 and 2 of the price control in Table 3.4 (see paragraph 3.63). As SONI will be progressing these via the Dt and Zt terms, the costs of the asymmetric risk should be included in the ARAt term.

SONI Position

- 3.37 SONI considers that without this adjustment we will be assuming risk for which we will not be recompensed as a direct result of UR's delays. This would be in contradiction of the CMA's 2017 Decision. SONI considers that the UR has failed to provide regulatory certainty.

¹⁰ Letter from Kevin O'Neill to Tanya Hedley on 21 May 2021

3.38 SONI requests that the UR recognises the additional risks and reflect the cost of these in the ARAt term in the licence modifications.

Key Issue 3.2: Effective Date for introduction of Conditional Cost Sharing Mechanism

- 3.39 SONI notes that there is no reference to a date for when the conditional cost sharing mechanism will apply.
- 3.40 Whilst SONI does not have visibility of the UR's timetable to complete the price control process, our expectation is that it will be well into 2022 before the process is completed when considering the statutory timelines. Based on this significant delay, SONI notes that the guidance documentation is unlikely to be in place to allow for the calculations of the Conditional Cost Sharing Mechanism terms (CSBA_t and CSCA_{Rt}) to be undertaken for Year 1 of the price control.
- 3.41 SONI considers that a pragmatic approach to this issue is to set both the CSBA_t and CSCA_{Rt} terms to zero for Year 1 of the price control. This should be included in the drafting of the licence.

SONI Position

- 3.42 The finalisation of the Conditional Cost Sharing Guidance is under an indeterminate timetable. SONI considers the UR's approach results in a number of errors:
- Failure to provide regulatory certainty
 - Failure to provide guidance and definitions necessary to assess whether the objective has been achieved
- 3.43 SONI requests that both the CSBA_t and CSCA_{Rt} terms are zero for Year 1 of the price control and the drafting of the licence is updated to reflect this..

Key Issue 3.3: Effective Date for introduction of Evaluation Performance Framework

- 3.44 In the Annex, paragraph (e)(ii) states In Relevant Year $t=3$ and all subsequent Relevant years, EP_t shall have a value.
- 3.45 SONI has been proactively preparing for the introduction of the Evaluative Performance Framework internally, however we consider that the implementation of the framework is dependent on:
- having the necessary licence arrangements and guidance documentation in place and published; and
 - having the independent evaluation panel established and functioning.
- 3.46 The Final Determination advises ".we [The UR] decided that it was not practical to apply the framework for the year from October 2020 to September 2021. We also continue to see

value in a transition year in which the framework would apply but without the application of financial incentives¹¹.”

- 3.47 SONI agrees that a transition year is necessary to ensure that the new processes are established and the end to end process is ‘tested’ prior to the application of any financial incentives. The Licence Modifications are based on the Evaluation Performance Framework being in place from October 2022 (start of Year 3). However, the UR has not considered the impact of the significant delay in progressing the licence modifications and the publication of final guidance documentation for the Evaluative Performance Framework. The process as it stands will not allow time for an adequate transition year. When considering the statutory timelines, SONI considers that the price control may be in place during Q1/2022 at the earliest. This leaves a maximum of 6 months for a ‘transition year’. SONI does not consider that this is practical as this time period will overlap with the preparation of the Year 3 assessments so the learnings from the transition period will not be available before the framework starts. SONI do not feel that the transition year should be lost simply as a result of the delays of the price control process.
- 3.48 In addition, SONI considers that for the framework to be successful, adequate time needs to be allowed for the Independent Panel to be appointed, become familiar with their duties and understand the activities they will be required to participate in. SONI has not considered the lead times required to have the Evaluation Panel recruited and in place in order to test the new processes end to end. This activity sits with the UR.
- 3.49 As a result of the above factors, SONI disagrees with the statement that the “*Relevant Year $t=3$ and in all subsequent Relevant Years that E_{Pt} shall have a value*”. SONI considers that it is in all parties (SONI, Independent Panel, Customers, Stakeholders and the UR) interests to have a full transition year without the application of financial incentives (as specified in the final determination).
- 3.50 Therefore, SONI proposes that the wording should be amended to advise “In Relevant Years $t=1$, $t=2$ and $t=3$, E_{Pt} shall equal zero” and “In Relevant Year $t=4$ and subsequent Relevant Years, E_{Pt} shall have a value”.

SONI Position

- 3.51 The finalisation of the Evaluation Performance Framework Guidance is under an indeterminate timetable. SONI considers the UR’s approach results in a number of errors:
- Failure to provide regulatory certainty
 - Failure to provide guidance and definitions necessary to assess whether the objective has been achieved
- 3.52 SONI requests that the wording should be amended to advise “In Relevant Years $t=1$, $t=2$ and $t=3$, E_{Pt} shall equal zero” and “In Relevant Year $t=4$ and subsequent Relevant Years, E_{Pt} shall have a value”.

¹¹ Para 4.37

3.53 SONI would welcome engagement with the UR to agree a plan for the transition year and the timeframes and processes in relation to the establishment of the Independent panel.

Trend of Delays in SONI Price Control Processes

3.54 For completion, SONI has noted a recurring trend with regards delays to its price controls. As shown in Table 3.2 below, it is important to note that the final decisions on the licence modifications for SONI’s last two price controls were published 24 months and 17 months after the start of each period respectively. As evidenced in Table 3.3, SONI has commenced seven of the last twelve tariff years without a codified revenue entitlement, introducing atypical operating challenges to the business. SONI is not aware of any other utility in the UK that has been subject to recurring delays of this nature and who has therefore been exposed to such periods of revenue uncertainty.

Table 3.2: Delays to SONI’s Price Controls

Price Control Period	Start Date	FD Published	Final Licence Mods Decision	Gap with revenue uncertainty
2010-15	1 Oct 2010	6 May 2011	11 Sept 2012	24 months
2015-20	1 Oct 2015	24 Feb 2016	14 Mar 2017 ¹²	17 months
2020-25	1 Oct 2020	15 Dec 2020	TBC	>13 months

¹² Excludes the CMA appeals process

Table 3.3: Tariff Years where SONI has had a codified revenue entitlement in place at the start

Tariff Year Beginning	Revenue parameters codified at start of tariff year
Oct-10	No
Oct-11	No
Oct-12	Yes
Oct-13	Yes
Oct-14	Yes
Oct-15	No
Oct-16	No
Oct-17	No
Oct-18	Yes
Oct-19	Yes
Oct-20	No
Oct-21	No

3.55 The undesirability of this situation was highlighted by the CMA in paragraph 8.8 of its final determination¹³ of SONI 2015-20 Price Control, where it stated:

“We consider that regulatory procedures, which create delay or uncertainty or both for the licence holder, are not in the interests of consumers as they may have adverse effects on the company’s ability to carry out its statutory functions associated with the transmission of electricity.”

3.56 SONI also notes that the Market Operator Licence that SONI holds has not had the decisions fully codified into the corresponding Annex 1.

3.57 SONI welcomes further discussion on these concerns with the UR ahead of the next price control process to ensure that the time frames set out by the UR are adhered to.

Key Issue 4: Hard Coded and Understated Value for Asymmetric Risk Premium (ARAt)

3.58 The UR has included a hard-coded value of £136k p.a. for SONI’s asymmetric risk in the Final Determination and draft licence modifications. This mirrors the CMA approach of allowing a 3% return to cover the recognised risk associated with SONI being limited to

¹³ <https://assets.publishing.service.gov.uk/media/5a09a73ce5274a0ee5a1f189/soni-niaur-finaldetermination.pdf>

recovering actual costs up to a cap. This relates specifically to costs in the Dt & Zt categories, network planning and TNPP expenditure.

3.59 In SONI's opinion, the UR has made an error in this calculation:

- Firstly, the UR has introduced two new uncertainty mechanism terms in these licence mods, Et & Vt. For items in these categories, the risk will be allocated symmetrically. However, due to the delays to the licence modifications, SONI will not be able to avail of these mechanisms during the first two years of the price control. The quantum of the ARAt term should therefore be increased to reflect the reality of the additional asymmetric risk imposed on SONI by the UR delay.
- In calculating the Asymmetric Risk Premium, the UR assumed a net annual allowance of £100K for the ENTSOE ITC function and the Interconnector Administrator function. This does not reflect the quantum of the UR approvals for these two items over the first two years of this price control. The risk being carried by SONI is clearly much higher than the level of revenue provided via the ARAt term. SONI considers that the actual risk should be reflected in the ARAt calculation. Therefore this line in the table should be a minimum of £649k p.a., as set out below.

3.60 When the SONI submission was made in 2019, the outcome of the Brexit process was still unknown, impacting projects that are required to align with the European Market. In particular, SONI highlighted two initiatives that were so uncertain that they could not be included within the business plan. These are:

- Initiative G13: Electricity Balancing Guideline (EBGL) refers to the resources required to apply the requirements of the EBGL to current balancing practices. SONI proposed that this will be treated as part of the uncertainty mechanism.
- Initiative G14: Multi-NEMO (Nominated Electricity Market Operators) Arrangements in the SEM will see the introduction of designated NEMOs into SEM. SONI proposed that this will be treated as part of the uncertainty mechanism

3.61 We would expect both of these initiatives to be processed through the Dt/Zt approach because of the magnitude of uncertainty and materiality of these costs. We note that the UR included a 'central estimate' of £250K per year to capture other Dt/Zt submissions. The rationale for this estimate is not clear in the Final Determination and estimate does not reflect the scale of costs that SONI expects to progress via the Dt/Zt uncertainty mechanisms.

3.62 These factors all understate the asymmetric risk that the UR is imposing onto SONI, with no offsetting factors. When combined over the five years, they combine to result in a material under-payment to SONI for the asymmetric risk. We therefore ask that this calculation is updated to correct for these clear errors and downward bias, as set out in Table 3.4 below.

Table 3.4 Calculation of ARAt

SONI TSO Price Control (2020-2025) Business Plan

Asymmetric Risk

DESCRIPTION

Forecast for SONI Price Control 2020-2025				
RELEVANT YEAR 2020-21 Apr-21	RELEVANT YEAR 2021-22 Apr-22	RELEVANT YEAR 2022-23 Apr-23	RELEVANT YEAR 2023-24 Apr-24	RELEVANT YEAR 2024-25 Apr-25

A	Cost Subject To Asymmetric Risk Allowance
1	Network Planning
2a	ENTSOE ITC Costs (Dt)
2b	Interconnector Administrator
2c	Increase in ENTSOE & CORESO Costs
3	Section 75 Pension Costs (Dt)
4a	Dt Requests made in Years 1 & 2
4b	Other Dt Items (UR Estimate for year 3+)
5	TNPP Spend
6a	Zt Requests made in Years 1 & 2
6b	Special Projects (Zt - UR Estimate for year 3+)
6c	Estimate for EBGL (as referenced in SONI Business Case)
7	Total [Capped Expenditure]
8	Annual average (years 3 - 5)
9	Asymmetric Risk Allowance
10	Asjtuement for asymmetric risk (Nt)

Note 1
Note 2
Note 3
Note 4
Note 5
Note 6

588	587	587	583	581
420	600	600	600	600
78	49	49	49	49
80	540	540	540	540
143	143	143	143	0
0	2,385	0	0	0
0	0	120	120	120
5074	3991	3300	2784	2150
209	7486	0	0	0
0	0	150	150	150
	500	?	?	
6,592	16,281	5,489	4,969	4,190
7,504	7,504	7,504	7,504	7,504
3.00%	3.00%	3.00%	3.00%	3.00%
225	225	225	225	225

Value of ARAt term

225

Note 1 Based on UR approvals of £420k in yr1 and 600k in yr2

Note 2 UR approval of £49k in year 2 - expect outturn to be approved in yr 1

	2020-21	2021-22	2022-23	2023-24	2024-25
	Apr-21	Apr-22	Apr-23	Apr-24	Apr-25
European Related Costs					
Estimated costs for ENTSO-E membership	90	350	350	350	350
Estimated costs for CORESO membership	200	400	400	400	400
Less Allowance	-210	-210	-210	-210	-210
Increase in ENTSOE & CORESO Costs	80	540	540	540	540

SONI ex-ante request of £90k for 2020/21 - request for 2021/22 out of date - £350k is low estimate

SONI ex-ante request of £200k for 2020/22 - request for 2021/22 out of date - £400k is low estimate

Note 4 **Value of Dts raised or to be raised in years 1 & 2**

	2020-21	2020-21	
	Apr-21	Apr-21	
Opex			
MIP Solver		6	Based on Submissions
Connections Disputes		175	
Moyle Control System		117	
RES		685	based on 'Future' Tab in FD Cost Allowances
Control Room Tools		188	
DRBC		300	
Physical Security		467	
Metering Systems		36	
Transforming Engagement		411	
Total Dt	0	2,385	

Note 5

	2020-21	2020-21	
Capex			
MIP Solver	186		Based on Submissions
Moyle Control System	23	471	
RES		2051	based on 'Future' Tab in FD Cost Allowances
Control Room Tools		1705	
DRBC		1745	
Physical Security		588	
Metering Systems		810	
Transforming Engagement		115	
Total Zt	209	7,486	

Note 6

Electricity Balancing Guidelines – this was considered too uncertain to include in the Price Control for both EirGrid and SONI

There is a deadline to have this in place by May 2024. SONI is actively working with the UR on the development.

It is expected that this will need to be funded via the Dt and Zt mechanisms due to the nature of the project (similar to iSEM)

Therefore an estimate should be included in the ARAt term

An estimate of £500k has been included in year 2, however the full value of this risk needs to be considered when the HLD is completed.

SONI Position

- 3.63 As indicated above, SONI would hold that the UR has not given full consideration to the impact the unavailability of the Et and Vt mechanism during the first two years of the price control has had on SONI's risk symmetry. SONI considers that the quantum of the ARAt term needs to be revised to take this into consideration. Therefore, SONI requests the calculation is updated and downward bias corrected as per the table above.
- 3.64 Of significance is the fact that this position and risk being attributed to SONI is contrary to the CMA's 2017 Decision. SONI considers that the UR's decisions and drafting creates a failure to provide regulatory certainty and expose SONI to risks and costs exposure.

Price Control Process

- 3.65 SONI has sought to work with the UR over the past three years to ensure that a robust process was followed for the delivery of this Price Control. SONI acknowledges that this process has been the most comprehensive review in relation to a SONI price control and there has been considerable resources applied to this exercise by SONI. We consider that there has been good engagement throughout the process leading up to the Final Determination.
- 3.66 However, we have identified three aspects of the process that undermine this consultation exercise and further impact the implementation of the Price Control itself. These are expanded upon below.

Key Issue 5: Unpublished Guidance Documents

- 3.67 The SONI TSO Licence Modifications make reference to three guidance documents (the "guidance"):
- Requirements and Guidance on Conditional Cost Sharing;
 - Requirements and Guidance on the Evaluative Performance Framework; and
 - Requirements and Guidance on Uncertainty Mechanisms.
- 3.68 At the time of publication of the UR Consultation on SONI TSO Licence Modifications, SONI had not been in receipt of a finalised version of the guidance documents. The UR however did provide a further updated draft version of these documents to SONI on 28 September 2021.
- 3.69 SONI is concerned that the fact that the guidance documents have not been published means that SONI and other stakeholders cannot fully assess whether the draft modifications achieve their stated effect and allow stakeholders to determine their impact. Some of the terms detailed in Annex 1 (e.g. CSBA_t, EPF, Et, Vt) are dependent on the various guidance documents in order to determine the revenue impact. As such, the referenced guidance documents are not 'traditional' guidance documents that could be produced during the life of a price control process. Rather, they are fundamental to

implementing the Final Determination. This suggests that the process undertaken by the UR is incomplete.

- 3.70 SONI is concerned that the dates from which the guidance documentation applies from should be defined in the licence or guidance documents - this remains an unknown.
- 3.71 SONI notes that the UR values to “*be a best practice regulator: transparent, consistent, proportional, accountable and targeted*”. SONI would interpret the transparent and consistent attributes as suitable rationale for publishing the finalised versions of the guidance document. SONI considers that the UR should follow the best practice procedures that it would apply to any other consultation process. These guidance documents formed part of a consultation process, and therefore the appropriate next steps in SONI’s opinion would be to then publish a decision or response paper alongside the finalised versions of the guidance documents.
- 3.72 SONI notes that in the Price Control Final Determination, Table 2: Supporting final determination documentation and guidance includes the three sets of guidance as key parts of the price control. In addition, Table 3: *Price control process timeline* indicates that the final stage in the process is ‘*Statutory licence modification statement and guidance decision*’. SONI considers that this reinforces the obligation that the documents should be published, and the UR has not followed its own processes.
- 3.73 The finalisation of the guidance on Uncertainty mechanisms, Evaluative Performance Framework and Conditional Cost Sharing is under an indeterminate timetable that SONI believes to be inadequate. Further, it is put forward that the Consultation cannot in fact be valid under Article 14(2) of the Electricity Order as the effect of these modifications cannot be considered without the guidance documents that the UR has failed to provide. Key stakeholders and consumers as a whole have not been afforded the opportunity to review documents which will have a fundamental impact on determining how these modifications operate. The absence of any consultation, or guidance as to their exercise, is a clear breach of the principle of “predictability”.
- 3.74 The Utility Regulator has a statutory ability to modify SONI’s Licence. It is also acknowledged and accepted that the Utility Regulator can publish guidance documents to facilitate understanding of how modifications (which have then become conditions) are to operate. However, if the modifications themselves and their ramifications are incapable of being understood on their own then such actions are ultra vires. In addition, deferring the operative mechanics of these modifications to guidance documents will prohibit SONI from having any appeal avenue.

SONI Position

- 3.75 In summary, SONI considers that the referenced guidance documents remaining unpublished is an error on a number of counts:
- Failure to achieve stated objectives via its failure to finalise a considerable amount of guidance material which are meant to drive the application of the requisite provisions of the price control.

- Failure to comply with the requirements of the Electricity Order by failing to introduce required guidance material which is needed to understand the effect of the proposed modifications.
- Failure to provide necessary material to understand the effect of the modifications does not comply with the requirements of a valid Article 14(2) Notice.
- To rely upon unpublished and non-consulted guidance documents and definitions to give effect to these modifications is ultra vires.
- The UR has introduced modifications which bypass The Gas and Electricity Licence Modification and Appeals Regulations (Northern Ireland) 2015 – by denying SONI and appropriate appeal route to decisions that will have a material impact on its operations.

3.76 SONI encourages the UR to set out a timetable for when the three sets of guidance referenced above will be published. SONI considers that these guidance documents should be published as part of a new Article 14 Notice process. SONI would welcome further engagement with the UR on the guidance documentation.

Key Issue 6: References to ‘Price Control Decision Paper’

3.77 There are 17 references¹⁴ to the “Price Control Decision Paper” throughout the draft Annex. SONI expects the Licence Modifications to be standalone and codify the UR Final Determination. A number of the requirements laid out in the Decision Paper are no longer applicable. For example:

- The Final Determination includes references to consultation documents (e.g. guidance documentation) that have not yet been finalised;
- The Final Determination includes reference to deliverables which are not defined;
- The Final Determination references some dates that have already passed (business cases for security related expenditure) thus making obligations retrospectively

3.78 SONI’s rights and obligations are set out in the Licence which incorporates Annex 1 – this is the purpose of the Licence. It is not appropriate for the Licence to direct the licensee to search for unclear rights and obligations by reference to a reading of the Final Determination and numerous Annexes. In addition to being contrary to good regulatory practice, it is particularly inappropriate given the inconsistencies between the Final Determination. SONI considers that the UR need to propose wording to fully transpose the Final Determination into the Licence. SONI is willing to support the UR in the development of this drafting.

¹⁴ SONI has addressed each of these individually throughout our response.

SONI Position

- 3.79 SONI considers that the approach undertaken by the UR is an error based on a failure to provide regulatory certainty and expose SONI to risks and costs exposure.
- 3.80 The open ended formal definition of "Price Control Decision Paper" means that subsequent decision papers relating to the price control can simply be incorporated by reference to the TSO Licence on an ongoing basis, without the need to implement any associated licence modifications and without offering SONI any opportunity to appeal such decision. SONI would consider this to be an unprecedented measure in UK regulation. In SONI's view, the requirement in Article 14(2) of the Electricity Order that the Utility Regulator gives notice setting out the proposed modifications and their effect has not been met in respect of this term.
- 3.81 SONI considers that the definition 'Price Control Decision Paper' and all references to it should be removed from the licence. We have commented on each of the 17 instances in section 4.3 of this paper.

Key Issue 7: Proposed Allowance Adjustments based on delivery

- 3.82 The Final Determination references an approach to adjustments to revenue based on non/partial delivery of deliverables, but it does not detail how these adjustments will be undertaken¹⁵.
- 3.83 This does not allow SONI the ability to quantify the risks that it is exposed to when making decisions, for example – alternative means of achieving the same end. SONI considers this to be a fundamental gap in the codification of the licence and the lack of guidance or procedure as to how the UR would undertake this assessment creates a significant risk to SONI.
- 3.84 This omission reflects a failure to detail the effects of the licence modifications and in order to correct this, definitions for adjustments to be made to allowances on the basis of non/partial delivery of deliverables would be required. Without this neither SONI nor any stakeholder can ascertain the effect of the modifications and therefore the UR has not met the requirements of a compliant Article 14 (2) Notice.
- 3.85 In considering the above issues, SONI would refer to the analysis the CMA conducted as part of the Provisional Determination on the series of appeals arising out of Ofgem's Final Determinations as part of the RIIO-2 process. In its Final Determinations, Ofgem considered that there is an expectation of outperformance in RIIO-2 and therefore proposed a 25bp downward adjustment to the CAPM-based cost of equity. This revenue adjustment is referred to as an 'outperformance wedge'. It was argued that the adjustment would undermine performance improvements and investment incentives, and increase regulatory risk.

¹⁵ Final Determination Annex 2 Paragraphs 3.5 to 3.9

3.86 The CMA has provisionally upheld the appeal concluding that Ofgem was wrong in introducing the outperformance wedge. The CMA considered that *'if introduced, might also undermine broader regulatory certainty which could result in increased costs to consumers over time.'* SONI considers that there is a read across to this issue as the current approach by the UR to a potential future undefined revenue adjustment leaves SONI exposed in a way that would undermine investors' confidence. SONI considers that the UR's proposition of adjustments based on performance would be interpreted in the same manner as the CMA provisional ruling in the above appeal.

SONI Position

3.87 The Licence modifications are silent on how this process would be applied to SONI. SONI's position is that there is a failure by the UR to provide the guidance and definitions necessary to assess whether the objective has been achieved and similarly, there is a failure to detail the effect of the licence modifications for this proposed adjustment.

Key Issue 8: Definition of Deliverables

3.88 As part of the final determination, the UR published a spreadsheet detailing the expected deliverables from the price control.

<https://www.uregni.gov.uk/publications/final-determination-soni-price-control-2020-2025>

3.89 This is referenced in paragraph 6.33 and 6.34 of the price control final determination and in Annex 2¹⁶.

3.90 SONI highlights the following concerns with the spreadsheet detailing the expected deliverables:

- 1) The deliverables spreadsheet is incomplete. There is yellow text included where the URs expectation appears to be that SONI will populate the spreadsheet. SONI notes that in the Final Determination that the UR states¹⁷ *'We will require SONI to further develop these over time. We expect development to be accounted for within our Evaluative Performance Framework.'*
- 2) The spreadsheet is highly granular and does not consider alternative solutions (e.g. it requests counts of various IT equipment (PCs, servers, firewalls etc.), but does not consider alternatives or substitutes (e.g. cloud-based solutions);
- 3) The template was not consulted on. The Draft Determination included a 'UR Output Monitoring' file which presented a much more high-level approach to reporting; and
- 4) The deliverables are not specifically referenced in the licence modifications. SONI considers this to be ambiguous and therefore creates uncertainty.

¹⁶ Annex 2 Services and Outcomes refers to this spreadsheet in paragraph 1.10 alongside footnote 1 referring to "UR Output Monitoring". This link takes the user to a page where it cannot be found.

¹⁷ Paragraph 6.34

3.91 SONI considers that the deliverables template as published is incomplete and therefore not fit for purpose. SONI considers that the significant change in both approach and detail required between the draft and final determination as not in keeping with good regulatory practice.

SONI Position

3.92 SONI has significant concerns in relation to the lack of definition surrounding deliverables associated with the allowances for the strategic initiatives and how these will be treated under both the Conditional Cost Sharing Mechanism and the Evaluative Performance Framework. SONI considers that this presents errors based on a failure to detail the effect of the licence modifications and a failure to provide guidance and definitions necessary to assess whether the objective has been achieved

3.93 Given the focus in the Final Determination of the performance of SONI during the price control, SONI expects that both the guidance documentation and any associated deliverables should be fully defined and documented up front such that all parties understand what is expected. The licence modifications should reflect this. SONI stresses the importance of clarity, consistency and transparency in the definition of deliverables within the licence modification process. We are available to support the UR in advancing this aspect of the price control.

Lack of Clarity in Final Determination and Modifications

Key Issue 9: Introduction of term “Manifestly Unreasonable”

3.94 The term ‘*Manifestly Unreasonable*’ has been introduced as part of the SONI TSO Licence Modifications with reference to:

- 1) The Cost Sharing Operating Expenditure Amount (CSB_t – Para 2.2d)
- And
- 2) The Closing Asset Value (CRAB_R_t – Para 2.3d)

3.95 However, no definition has been provided within the Definition and Terms of the Annex document. Therefore, there are no set parameters by which to determine whether or not an item is “*Manifestly Unreasonable*”.

3.96 The calculation for this amount CSB_t (Para 2.2(d)) is given by the formula:

$$CSB_t = [AO_t - B_t] \times 75\% + CSBA_t$$

3.97 The AO_t term, being the relevant actual operational expenditure in year t, is the term that is notably affected by the conditions 2.2 (d) (B) 1) and 3) (see below), whereby it will be adjusted (reduced) by the amounts, as determined by the UR, deemed Demonstrably Wasteful or Inefficient (DIWE) *and/or* manifestly unreasonable.

3.98 Para 2.2 (d) states:

(B) *the sum of the amounts attributable to each of the following items:*

- 1) *that part (if any) of such costs that the Authority determines at any time to be Demonstrably Inefficient and Wasteful Expenditure;*
- 3) *any part of such costs which the Authority may determine from time to time to be manifestly unreasonable to include in costs which are subject to the cost sharing arrangements;*

3.99 In addition, the term is also included within the Closing Asset Value (CRAB_Rt – Para 2.3d), and specifically the CSC_Rt term whereby it is calculated by the following formula:

$$CSC_{R_t} = [AC_{R_t} - C_{R_t}] \times 75\% + CSCA_{R_t}$$

3.100 Similarly, to the AOt term, the manifestly unreasonable condition will affect the AC_Rt term for Actual Capital expenditure in year t.

3.101 Whilst the Utility Regulator has referenced such a term being contained within NIE Networks Licence, no similar terms are found in other transmission licences in the jurisdiction, nor in comparable GB licences. The reasoning that such a term is designed to create regulator parity with NIE Networks does not make sense. The term has existed within the DNO's & TAO licences for some time. As such, the Utility Regulator has had opportunities to amend SONI's licence to account for it, but has not. Further, it is not a replication of NIE's Licence condition which includes the requirement for the Utility Regulator to make a published decision.

3.102 At present the SONI Licence provides for adjustments in actual operational expenditure, as a result of (DIWE), under para 2.2 (c) (i) (A), but does not include an additional adjustment for expenditure deemed manifestly unreasonable.

3.103 This new term appears to overlap with and therefore, contradict the existing DIWE condition. This condition and its operation received extensive review by the CMA as part of its 2017 Decision. The Utility Regulator has not published any evidence or material that indicates that this condition is not functioning as intended and therefore ought to be replaced. Instead it has introduced a parallel condition with no substantive guidance as to when each or either is to apply

3.104 Furthermore, the parameters and management of implementing operational adjustments resulting from DIWE, is determined in accordance with the UR's published (July 2017) document *Guidance on the interpretation and application of the Demonstrably Inefficient or Wasteful Expenditure (DIWE)*. This detailed document benefits both the UR and the Licensee in that it provides clarity and understanding in the approach and processes to be applied in determining the exclusion of expenditure deemed inefficient or wasteful.

3.105 It is important to note the procedural element of the DIWE guidance (See flow chart below). This highlights that any deduction imposed on SONI will be as a result of a fair and detailed assessment and ensures the licensee (SONI) has a right to reply and provide evidence that may mitigate any DIWE penalty.

3.106 Without this procedure, or any similar corresponding guidance in relation to manifestly unreasonable costs, SONI is exposed to being financially penalised in an imbalanced, one-sided manner, without any right to challenge or appeal.

3.107 SONI notes that the UR stated in the consultation paper that

'The effect of the drafting is to remove unreasonable costs from sharing calculations. This might include items which are not demonstrably inefficient but shouldn't be paid for by customers e.g. company fines.'

3.108 SONI has completed a worked example where the DIWE process has been applied to a scenario where SONI has incurred a 'company fine'. As demonstrated below, SONI considers that this scenario is adequately dealt with using the clearly defined procedures in the DIWE guidance. Therefore, SONI fails to see when a scenario would arise where the 'manifestly unreasonable' terms would apply rather than DIWE.

Worked Example

3.109 The following hypothetical example highlights the procedural steps and resulting actions that clearly demonstrate a fair and reasonable resolution in evaluating SONI expenditure which may be considered DIWE.

Working Hypothetical Example - Summarising procedure and possible outcomes of SONI Ltd being subject to a Company fine levied as a result of its Operational Activities

DIWE Procedural Elements	Actions
<p align="center">Procedure to Determine application of Detrimental Wasteful or Inefficient Expenditure Condition</p>	<p align="center">SONI includes cost of fine within its Maximum Tariff Revenue calculations, under the AOT term, with a view to it being recovered through the tariff</p>
<p>The UR will decide in its discretion whether or not to undertake an assessment of whether specified expenditure is DIWE. It may do so in particular where information has come to the attention of the UR that expenditure incurred by the Licensee might be DIWE</p>	<p>The UR, as part of its review of the RIGs (CCS Step 2-4), queries the legitimacy of SONI including the cost of the fine as part of its AOT term. The UR considers the fine to potentially fall under DIWE.</p>
<p>The UR will usually seek to notify the Licensee as soon as reasonably practicable if it decides to assess whether any expenditure is DIWE. However, it reserves the right to carry out an assessment at any time without such notice having been given</p>	<p>The UR informs SONI of its decision that it will be assessing this expenditure (SONI's payment of fine) with a view that it may not be approved under the terms of the DIWE guidance</p>
<p>The UR will follow such procedures as it considers appropriate in each case for the purpose of determining whether expenditure is DIWE. These may include the use of any audit, assessment or consultation in respect of the expenditure and the conduct of the Licensee and/or its third party contractors in relation to it</p>	<p>The UR conducts an assessment of the fine in accordance with Paragraph 13 c) of the DIWE Guidance, including but not limited to:</p> <ul style="list-style-type: none"> - the reasons for the fine being levied - consultation with relevant body imposing the fine - consultation with industry experts (Legal, financial, SMEs etc) - assessment of SONI acting outside its operational remit - review relevant legal frameworks and legislation - consideration of fine to be justifiably recovered through tariff
<p>In considering whether expenditure is DIWE, the UR will have regard to all relevant information submitted by the Licensee, and may request further information as part of its review.</p>	<p>SONI Ltd provides all relevant information to UR detailing how the fine should be recovered through the tariff as an element of its actual expenditure (AOT), including but not limited to, for example:</p> <ul style="list-style-type: none"> - legal justification for inclusion in tariff - legitimacy of the fine itself - necessary operational requirements resulting in fine - current ongoing legal engagement disputing the fine
<p>Where it identifies expenditure that it considers may be DIWE, the UR will invite the Licensee to make representations, and will take those representations into account before making its final determination</p>	<p>SONI is given the opportunity to make representations based on the information it has previously provided, whilst utilising any other additional relevant information that has come to light as part of the on-going process</p>
<p>Where the UR determines that any expenditure is DIWE, it will, in accordance with the definition of that term, provide the Licensee with reasons for its decision</p>	<p>The UR concludes its assessment and makes a fair and informed decision as to whether the fine should be considered DIWE. The UR provides SONI with a detailed reasoning behind its decision. If required, the cost of fine is removed from the AOT calculation in line with Annex 1 paragraph 2.2 (d) (ii) (B) 1)</p>

SONI Position

- 3.110 Upon review of the current DIWE guidance, and in particular the procedures as set out above, SONI has concluded that there would be no relevant scenario whereby the UR would have to reference the manifestly unreasonable term, that wouldn't already be captured under the DIWE conditions.
- 3.111 SONI also notes that the term 'manifestly unreasonable' does not have an agreed definition in case law. In a regulatory context, SONI has only found its use by Ofgem in the context of customer backbilling. Its use by the UR in the context of costs analysis appears to be a creature of its own creation. SONI therefore considers that its use would lead to future disagreements and challenges. Therefore its inclusion would undermine the purpose of the well understood and accepted DIWE process and guidance.
- 3.112 SONI considers that the UR's approach is an error as it fails to provide regulatory certainty
- 3.113 As such, we would request that the wording is removed in its entirety from the AOT term and the AC_Rt term.

Key Issue 10: INCENTt Term & Deletion of DBC related definitions

- 3.114 The UR has proposed the deletion of the 'INCENTt' term and the definitions associated with the Dispatch Balancing Costs Incentive included in Annex 1¹⁸. SONI notes that the deletion of these definitions and the INCENTt term does not appear to be referenced or signalled in the Final Determination.
- 3.115 The SONI Licence was updated at the start of the previous price control to codify a SEM Committee decision to implement an incentive on SONI and EirGrid to reduce dispatch balancing costs¹⁹. The magnitude of these costs was too difficult to predict over the early years of the new trading arrangements (I-SEM), so the SEM Committee decided to pause the mechanism.
- 3.116 The proposed licence modifications are premised on an incorrect assumption that this pause is permanent and the UR is therefore proposing to remove the references to Dispatch Balancing Costs that are contained in the annex. However, no corresponding changes are proposed to Condition 39 in the SONI Licence, which cross references the Annex for definitions of terms that will continue to apply under the reporting requirements.
- 3.117 The UR's reasons & effects relating to the proposed deletion are that 'the DBC incentive is no longer required' and that it 'tidies the licence'. The INCENTt term is also referred to as 'defunct'.
- 3.118 SONI notes that the UR has not made reference to a SEM Committee decision in relation to this incentive arrangement. Indeed, the assumption made by the UR that this incentive is no

¹⁸ Definitions marked for deletion are Dispatch Balancing Costs, Energy Imbalances, Ex Ante DBC Target, Ex Post DBC Target, Ex Post Adjustment, SEM Decision Paper, SO Interconnector Trade, Uninstructed imbalance

¹⁹ <https://www.semcommittee.com/news-centre/incentivisation-all-island-dispatch-balancing-costs-decision>

longer required directly contradicts a letter received by the TSOs which was sent on behalf of the SEM Regulatory Authorities²⁰ on 9 March 2021, which states that:

“In relation to the TSOs’ request for clarity on the RAs’ approach for Imperfection Incentives in tariff years beyond 2019/20, please note that this matter is subject to ongoing consideration by the RAs. Notwithstanding, the RAs note that any potential update to the current Imperfections Incentive Mechanism (as set out in SEM-12-033) would require a public consultation, and would need to be included in the RAs annual work programme (currently not included in the RAs’ 2021 work programme).”

The RAs will continue to consider the merits of including this potential work item in its future work programmes, and in the interim would welcome any further observations from the TSOs regarding the merits of continuing with an Imperfections Incentive Mechanism and potential amendments to SEM-12-033.”

3.119 Such proposed modifications do not come within the scope of the Notice as they do not give effect to the Final Determination, and there is no legal basis on which the Licence can be modified in this regard under the current consultation.

3.120 SONI would refer to the SONI Price Control Final Determination 2015-2020 where the UR provides a summary of components in Section 1.2, paragraph 11 including:

“INCENTt relates to the SONI portion of the all-island Dispatch Balancing Cost Incentive reward/penalty. This reflects the SEM Committee ‘Incentivisation of All island Dispatch Balancing Costs’ decision for which licence modifications were published in August 2015”

3.121 SONI highlights that the UR indicated in the above, that this is a consequence of a SEM Committee decision. The SEM Committee has not reversed this decision, or published a modification to amend this decision. SONI considers these two actions as the only rationale acceptable in order to remove this requirement from the SONI TSO Licence as this ultimately should only transpire to make effective any a decision made by the SEM Committee in this matter.

SONI Position

3.122 SONI therefore requests that these definitions and the associated algebra are reinserted into the Annex because:

- The UR would be acting ultra vires by removing them as its removal should be as a result of a SEMC decision, which has not yet been consulted upon.
- Condition 39 is rendered incomplete without them,
- The reasons and effect paper does not highlight the deficiency created in Condition 39,
- For these reasons, the UR's actions amount to an error in law.

²⁰ Letter from David Egan to Sam Matthews ref: D/21/5654 of 9 March 2021.

Key Issue 11: Selection of Uncertainty Mechanism for Additional Approved Costs

- 3.123 Under paragraphs 8.6 and 8.7, the drafting states that the UR will determine which of the four uncertainty mechanisms will be used for approval including the option of using a combination of the mechanisms.
- 3.124 The Dt and Zt terms will provide funding up to a 'cap'. The 'cap' approach does not provide an outperformance opportunity. The Et and Vt terms will provide funding based on a defined allowance and the mechanistic risk share (75:25) will apply to any over/under recovery. The current drafting does not consider the risk profile of the SONI submissions. For example, SONI may consider a project has elements of uncertainty (in terms of costs or timing) and therefore requests a cap (using Dt or Zt term). This approach allows SONI to deliver the project and recover its actual costs. In addition, during the project, SONI can submit a request for the cap to be increased (based on a robust justification). SONI will have relied on this provision when making its submission, and will therefore have excluded costs that may arise under some circumstances, knowing that it has the ability to rely on the uplift mechanism to mitigate the risk.
- 3.125 Out of the four mechanisms that the Utility Regulator has afforded itself, minimal detail is provided as to when one is to be used over another. SONI seeks clarification on the criteria the UR will use in making this decision. The licence modifications are silent on the risk profile being applied when SONI make a submission. This is a significant concern for SONI. For example, SONI may submit a Zt request for a project reflecting the uncertainty of the costs associated with the project. Based on the current drafting, the UR could determine an approval using Vt with a specific allowance and the use of the mechanistic cost sharing arrangement with no ability for SONI to challenge or appeal that decision, or even the opportunity to update its request to reflect the cost risks that it had not included within the original submission, but that it is now exposed to under the Vt approach.

SONI Position

- 3.126 There is a failure to provide regulatory certainty as to how a submission will be treated, and therefore this exposes SONI to risks and cost exposure. SONI could be left in the position whereby the Utility Regulator could determine an approval based on an allowance rather than a cap that can be uplifted as uncertainties become known. This would expose SONI to a risk of an overspend and the financial impact of having to fund 25% of any overspend, which SONI may have no control over;
- 3.127 One of the UR's core values is around transparency, and SONI requests that the effects are detailed in a clear manner in the guidance documentation, alongside a clear process as to when each of the general uncertainty mechanisms is appropriate for selection when preparing a submission to the UR.

Key issue 12: AOt Definition and AC_Rt Definition

- 3.128 AOt is defined as: 'the actual Operating Expenditure incurred in Relevant Year t by the Licensee insofar as the expenditure is incurred in the performance of its activities that are

authorised by or subject to obligations under the Licence....'. SONI considers that this wording fails to provide complete clarity over the costs covered in this area, leaving it open to ambiguity and it does not achieve its stated objectives.

3.129 SONI remains unconvinced by the need and basis for which the UR has put forward for this modification.

3.130 Throughout the Price Control Process, the Utility Regulator has emphasised that one of the intended objectives is to "*support SONI in delivering whole system outcomes*". The notion of "whole system outcomes" would appear to give acknowledgement to the fact that SONI has a wide range of legal duties and responsibilities which extend beyond those detailed within its Transmission Licence.

3.131 The current drafting is such that SONI will be unable to recover the actual costs for activities that are not specifically defined within its Licence, even though some of these have been explicitly funded by the UR through this price control process. We do not consider that this was an intended outcome by the UR when drafting the licence modifications. Examples of where such obligations arise that are not defined in the SONI licence and therein associated costs will be incurred include:

- Cyber Security;
- EU Network Code Implementation (including Common Grid Model and new arrangements for the procurement of System Services);
- Ongoing operation of methodologies developed and/or approved under the Network Codes;
- Work supporting the DfE, including the development of its Energy Strategy and publication of a winter outlook report;
- Proactive work to decarbonise the electricity system, that goes beyond basic priority dispatch (for example there is no licence obligation which requires SONI to proactively increase SNSP);
- Membership of ENTSO-E and CORESO; and
- REMIT and other transparency initiatives.

3.132 Without the ability to recover costs for these obligations, SONI runs the risk of being unable to achieve them. In such a scenario SONI would be in position of breaching the legal obligations imposed on it, which in turn would mean that the Utility Regulator may be in breach of its statutory duties. As such there is no possible way that the current drafting can be deemed to support SONI in achieving whole system outcomes and therefore fails to account for the roles and responsibilities of SONI.

SONI Position

3.133 SONI's position is that the current definition does not cover the full suite of legal obligations that SONI will need to incur costs against in order to fulfil its duties, and therefore considers there is an omission in the current drafting. SONI considers this omission is an error on the basis of:

- failure to take into account the full extent of SONI's obligations in the Licence Modifications

3.134 SONI is available to support the UR in the necessary drafting of both of these terms.

4 SONI Concerns Relating to Licence Modifications

4.1 This section follows the format of the draft paragraphs of Annex 1 of the licence. SONI has provided our comments on each sub paragraph. We have also included our comments on the reasons & effects as detailed in the Article 14 Consultation paper.

Paragraph 1 - Definitions

Definition	SONI Comments
Dispatch Balancing Costs Energy Imbalances Ex Ante DBC Target Ex Post DBC Target Ex Post Adjustment SEM Decision Paper SO Interconnector Trade Uninstructed imbalance	<p>These 8 definitions have been removed from the drafting licence. These are discussed further under Key Issue 10: INCENT Term & Deletion of DBC related definitions.</p> <p>SONI considers that these definitions should be reinstated.</p>
Price Control Decision Paper	<p>SONI considers that this term is not required as the licence modifications should be stand alone and codify the Final Determination.</p> <p>This is discussed further under Key Issue 6: References to 'Price Control Decision Paper'.</p>

Definition	SONI Comments
<p>Requirements and Guidance on Uncertainty Mechanisms</p>	<p>SONI notes the following wording included in the Reasons and Effects table:</p> <p><i>‘The amendment will improve clarity and better reflect our approach of remuneration of costs incurred by SONI up to an approved cap as this applies to opex and capex.’</i></p> <p>SONI considers that the wording ‘up to an approved cap’ is incorrect and does not reflect the range of uncertainty mechanisms referenced in Paragraph 8.6 and the guidance document. SONI requests that this is clarified by the UR.</p> <p>This definition is also discussed further under Key Issue 5: Unpublished Guidance Documents.</p>
<p>Requirements and Guidance on Conditional Cost Sharing</p>	<p>SONI considers that part (e) of this definition should be removed.</p> <p><i>(e) such other matters as appear to the Authority to be expedient for the purposes of giving effect to, and facilitating the operation of, the conditional cost sharing arrangements as more fully described in the Price Control Decision Paper.</i></p> <p>The Guidance Document should stand alone and be such that the Conditional Cost Sharing mechanism is predictable and clear in terms of implementation.</p> <p>The UR has awarded itself the ability to update the guidance and therefore the reference back to the Price Control Decision Paper is not required.</p> <p>The Price Control Decision paper references out to the draft Conditional Cost Sharing guidance which has not been finalised and therefore we consider that the Final Determination is not an appropriate reference (examples below);</p> <p>Final Determination - Para 5.40</p> <p><i>We produced a draft guidance document for the application of the conditional cost sharing approach, which we are publishing today for consultation alongside our final determination.</i></p> <p>As a general point, there are numerous occasions in the Final Determination where the UR has referenced back to the Draft Determination (e.g. ‘adopt the scope of the conditional cost sharing approach proposed in our draft determinations’) which may introduce additional complications/lack of clarity if the references to the Price Control Decision Paper remains. The reliance on documents where matters have</p>

Definition	SONI Comments
	<p>been updated to reflect the outcome of consultations raises a risk that there is potential for conflict between them.</p> <p>This definition is also discussed further under Key Issue 5: Unpublished Guidance Documents.</p>
<p>Requirements and Guidance on the Evaluative Performance Framework</p>	<p>SONI considers that part (e) of this definition should be removed from this definition.</p> <p><i>(e) such other matters as appear to the Authority to be expedient for the purposes of giving effect to, and facilitating the operation of, the evaluative performance framework as more fully described in the Price Control Decision Paper.</i></p> <p>The Guidance Document should stand alone and be such that the Evaluative Performance Framework mechanism is predictable and clear in terms of implementation.</p> <p>The UR has awarded itself the ability to update the guidance and therefore the reference back to the Price Control Decision Paper is not required.</p> <p>The Price Control Decision paper references out to the draft Evaluative Performance Framework guidance which has not been finalised and therefore we consider that the Final Determination is not an appropriate reference (examples below);</p> <p>Final Determination - Para 4.2</p> <p><i>We provide our detailed position on the Evaluative Performance Framework in Annex 2, along with other price control arrangements, to ensure that SONI is accountable for its performance and its delivery. We are also consulting today on our Evaluative Performance Framework guidance</i></p> <p>Annex 2 – 3.12</p> <p><i>More detailed information on our approach to the treatment of price control deliverables within the evaluative performance framework provided in the draft guidance we are publishing alongside our final determinations</i></p> <p>Annex 2 – 2.46</p> <p><i>..... For instance, the panel should not use its assessment to reward or penalise SONI simply for under-spend or over-spend on costs subject to conditional cost sharing. The draft guidance we have developed for that framework confirms this limitation on the scope of the evaluative performance framework</i></p>

Definition	SONI Comments
RPI	<p>The term RPI is used in the calculation for the PCR_t (2.6) and DEP_SPT (2.7) terms, however the definition is not included in the draft modifications. This needs to be added. Proposed text below based on existing licence.</p> <p><i>RPI means the Retail Price Index (1987 = 100) published or determined with respect to April in Relevant Year t (i.e. RPI in the Relevant Year t = 2 means the value of RPI in April falling within the Relevant Year t=2);</i></p>

Paragraph 1.2

4.2 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2 Restriction of SSS/TUoS Charges

Paragraph 2.1 – The Restriction:

4.3 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.2 - The Maximum Core Revenue (MC_t)

4.4 Under the MC_t formula, SONI notes a number of changes and the inclusion of new terms. SONI notes however that the UR has removed the term INCENT_t. In line with our comments above on the definitions associated with the DBC incentive, we consider this term needs to be reinstated into the MC_t formula. This is discussed further under **Key Issue 10: INCENT_t Term & Deletion of DBC related definitions.**

Paragraph 2.2 (a) The Pass-Through Amount (A_t)

4.5 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.2 (b) - The Ex Ante Allowance for Operating Expenditure Subject to Cost Sharing (B_t)

4.6 SONI considers that the ex-ante allowances for BO_t and UO_t are clearly stated in table A. Therefore, the reference to the 'Price Control Decision Paper' is unnecessary and should be removed. For further information see **Key Issue 6: References to 'Price Control Decision Paper'**.

4.7 In addition, SONI is concerned that there is insufficient transparency as the figures in table A in Annex 1 are not directly presented in the Final Determination. The Reasons & Effects

table references the relevant narrative in the Final Determination but does not cover how the allowances stated in Table A are derived. In the interests of transparency, SONI considers that the UR should publish a reconciliation between Table A and the tables included in the Final Determination.

Paragraph 2.2 (c) - The Pension Deficit Repair Amount (PRt)

- 4.8 SONI considers that the ex-ante allowances for the term PDRt is clearly stated in table B. Therefore, the reference to the 'Price Control Decision Paper' is unnecessary and should be removed. For further information see **Key Issue 6: References to 'Price Control Decision Paper'**.

Paragraph 2.2 (d) The Cost Sharing Operating Expenditure Amount (CSBt)

- 4.9 SONI has a number of concerns in relation to various aspects of the drafting and formulae included in this sub paragraph. Each of these are addressed below.

References to Price Control Decision Paper (CSBt):

- 4.10 SONI failed to find any references to the '*principles and subject to the conditions*' relating to the cost sharing arrangements (CSBt) in the main Price Control Decision Paper or Annex 3. The majority of references relate to the conditional cost sharing arrangements (CSBat), which has related draft guidance that the UR is consulting on as part of the Final Determination publication.
- 4.11 To avoid ambiguity and to ensure the Final Determination is codified in the licence, SONI considers that the reasons & effects and the licence should detail the '*principles*' and '*conditions*' associated with the CSBt term. The reference to the Price Control Decision Paper should be removed. This will ensure the treatment is transparent and predictable. For further information see **Key Issue 6: References to 'Price Control Decision Paper'**.

References to Price Control Decision Paper (AOt) sub paragraphs A1 and A9:

- 4.12 SONI considers the wording in sub paragraphs A1 and A9 under the AOt term to be incorrect and confusing for the following reasons:
- a) The Ex ante allowances for Operating Expenditure is specified in table A.
 - b) SONI failed to find any reference in the Final Determination to the term '*cost categories for the Licensee's overheads or support functions*'. SONI considers that the licence modifications should be clear in terms of the intended treatment of costs and the specific categories that these costs may fall into.
 - c) The current wording suggests that any costs relating to overheads or support functions cannot be assigned to transmission networks planning activities or connection charges. We consider this is not the URs intention and we seek clarification on the intended treatment of costs.

4.13 The references to the Price Control Decision Paper in sub paragraphs A1 and A9 should be removed. This will ensure the treatment is transparent and predictable. For further information see **Key Issue 6: References to 'Price Control Decision Paper'**.

Limitations of AOt Definition

4.14 AOt is currently defined as: 'the actual Operating Expenditure incurred in Relevant Year t by the Licensee insofar as the expenditure is incurred in the performance of its activities that are authorised by or subject to obligations under the Licence....'

4.15 SONI has many obligations that are created outside the licence framework and that are not transposed into it because they apply by automatic application of the law.

4.15.1 We have discussed our concerns regarding this definition under **Key issue 12: AOt Definition and AC_Rt Definition**.

AOt – Any other costs (sub paragraphs A8):

4.16 SONI note the inclusion of the wording: 'any other costs recoverable by the Licensee under the terms of the Maximum Core Revenue calculation at paragraph 2.2 above besides the Bt and CSBt terms; and '

4.17 SONI has assessed each of the terms in the calculation of MCt and do not consider that this term is required. For example, considering each term under Maximum Core Revenue:

- EP & NIA don't apply as they are not opex costs;
- K is revenue related;
- Nt is finance related;
- BNBt, Zt, PCR, AB_PC are all capex related.

4.18 SONI would like the UR to indicate the scenarios where this drafting may apply to. The UR provided the following effect for this drafting – "*This incorporates a catch-all for any other costs which are recoverable under other licence terms*".

4.19 SONI considers that the licence should be clear on each aspect of the price control. All parties should understand how all costs are to be treated in the revenue calculations. Therefore, the use of '*catch all*' terms should be avoided. SONI considers that this drafting should be removed.

Manifestly Unreasonable (sub paragraphs B3):

4.20 The draft licence modifications include details of actual costs which are to be adjusted to remove specific costs that sit outside the cost sharing arrangements (e.g. TNPP costs, connections, pension deficit etc). The following text has been included under sub paragraph B3: '*any part of such costs which the Authority may determine from time to time to be*

manifestly unreasonable to include in costs which are subject to the cost sharing arrangements;

- 4.21 SONI is concerned that this wording overrides the DIWE calculation and may allow the UR to make any adjustments they wish with no ability for SONI to challenge or appeal. SONI considers that the licence modifications should be such that the treatment of costs is predictable from the outset.
- 4.22 For further information see Key Issue 9: Introduction of term “Manifestly Unreasonable”.

Paragraph 2.2 (e) The Evaluative Performance Framework Amount (EPt)

- 4.23 SONI has three key concerns in relation to the Evaluation Performance Framework. These are listed below and addressed in order:
- 1) Inclusion of commercial terms in the guidance document rather than the licence
 - 2) Date at which the Evaluation Performance Framework is effective from
 - 3) Dependency on Independent Evaluation Panel

Inclusion of commercial terms in the guidance document rather than the licence

- 4.24 SONI notes that the EPt term in the draft licence refers to guidance documentation ‘*Requirements and Guidance on the Evaluative Performance Framework*’. SONI notes that the UR can change this guidance with no mechanism for SONI to appeal these changes. As this guidance has direct implications on the revenue available to SONI, we consider that SONI is exposed. For example, the UR could change the range of values included in the incentive scheme via a change to the guidance documentation.
- 4.25 SONI considers that this risk can be mitigated by the inclusion of the commercial ranges of the incentive arrangements in the drafting of Annex 1 of the licence. SONI proposes the following drafting:
- 4.26 Add to the definition for ‘The Evaluative Performance Framework Amount’ (EPt) (2.2 (e))

The incentive amount EPt will be calculated as follows using the methodology as may be set out in the Requirements and Guidance on the Evaluative Performance Framework:

If the overall grade is above 3, then EPt will be calculated as the overall grade minus 3, multiplied by £800,000. This will be a positive number, indicating a financial reward under the incentive scheme.

If the overall grade is below 3, then EPt will be calculated as the overall grade minus 3, multiplied by £375,000. This will be a negative number, indicating a financial penalty under the incentive scheme.

If the overall grade is 3, then EPt will equal zero.

Date at which the Evaluation Performance Framework is effective from

- 4.27 SONI has detailed our comments in Key Issue 3.3: Effective Date for introduction of Evaluation Performance Framework.

Dependency on Independent Evaluation Panel

- 4.28 SONI considers that the Evaluative Performance Framework will work effectively only when there is an established Evaluative Panel in place. We consider this as a prerequisite for the operation of the Evaluative Performance Framework. In addition, the guidance is unclear in terms of what happens if there is no evaluative panel in place (e.g. no quorum during the price control period). SONI considers that clarifications should be included in the licence and relevant guidance to reflect these concerns and ensure that all stakeholders understand the actions that take place in these scenarios.

Paragraph 2.2 (f) The Net Incentive Adjustment Amount (NIAt)

- 4.29 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.2 (g) The Dt Uncertainty Mechanism Amount (Dt)

- 4.30 SONI has no comments on the definitions in this sub paragraph; however we would highlight our concerns regarding the treatment of actual operational expenditure pertaining to items within the Dt uncertainty mechanism. This is explored and discussed in further detail below in para 4.32 – The Correction Factor (Kt).

Paragraph 2.2 (h) The Network Planning Scoping and Feasibility Amount (SFt)

- 4.31 SONI considers that the ex-ante allowances for SFPt are clearly stated in table C. Therefore, the reference to the 'Price Control Decision Paper' is unnecessary and should be removed. For further information see **Key Issue 6: References to 'Price Control Decision Paper'**.

Paragraph 2.2 (i) The Correction Factor (Kt)

- 4.32 SONI requests the definitions contained within this section of the Annex are revised to ensure that allowances for additional Opex costs, approved through the Dt uncertainty mechanism, are appropriately recovered by SONI. Presently the proposed treatment of Dt costs and allowances could impact the Kt factor in a manner that is unsound and indeed contradictory to the underlying logic and rationale attributed to approved Dt allowances.

- 4.33 In accordance with Para 8.8 and the Draft Uncertainty Mechanism Guidance document, the Dt allowances facilitate the spending of additional Opex by SONI up to a maximum (capped) amount. This total, maximum amount, given the specific nature of the Dt Opex requested, may be incurred by SONI over a number of years and as such, the UR would approve Dt maximum allowances for each year t that is applicable to the project.
- 4.34 It is the treatment of these capped allowances and specifically the relevant Dt actual operational expenditure, within the Kt correction factor formula, as detailed in the examples below, that requires further examination from the UR.
- 4.35 The structure of the Dt uncertainty mechanism is such that it should facilitate SONI to recover certain approved Opex costs up to an approved total capped amount. However, the process to facilitate the recovery of these costs based on the current drafting is flawed, as there is the potential for SONI not to avail of these allowances even if the maximum cap has not been reached.
- 4.36 For example – Dt Project A has approved total allowances of £180k, broken down into £100k allowance in Year t1, £40k in Year t2 and £40k in Year t3. In the event that the project has a different cost phasing in reality, the actual expenditure profile may show no expenditure in Year one and continue as follows:

Profile 1

Example - Dt Project A (£'000)	Year t1	Year t2	Year t3	Year t4	Year t5	Total
Approved Dt Project A allowances	100	40	40	0	0	180
Actual Dt Costs	0	70	60	20	0	150
Returned to customers through Kt Correction Factor	-100	0	0	0	0	-100
SONI Unrecoverable Losses	0	30	20	20	0	70

Summary for Dt Project A	(£'000)
Income Received through Tariff	180
Returned to customers through Kt Correction Factor	100
Net Allowances	80
Actual Costs	150
SONI Net Losses	-70

- 4.37 As the tables above show, this is an instance where SONI expenditure did not reach the maximum cap of £180k (only £150k spent), however, because the project spending profile altered, SONI was unable to recover £70k.

4.38 In addition to this scenario, let us assume the same Opex but the phasing occurs in the same years as the approvals and thus Opex spent in the appropriate years, as follows:

Profile 2

Example - Dt Project A (£'000)	Year t1	Year t2	Year t3	Year t4	Year t5	Total
Approved Dt Project A allowances	100	40	40	0	0	180
Actual Dt Costs	70	60	20	0	0	150
Returned to customers through Kt Correction Factor	-30	0	-20	0	0	-50
SONI Unrecoverable Losses	0	20	0	0	0	20

Summary for Dt Project A	(£'000)
Income Received through Tariff	180
Returned to customers through Kt Correction Factor	50
Net Allowances	130
Actual Costs	150
SONI Net Losses	-20

4.39 Although not as financially damaging, again this example highlights how the mechanism is flawed, because £20k of Opex would be disallowed/unrecovered even though the maximum cap allowance (£180k) was not reached by SONI (actual Dt Opex of £150k).

4.40 SONI considers it is not unreasonable to recover all Dt Opex costs as required, up to the total Dt project amount approved, regardless of changes to Opex spending profiles, as detailed in the examples above.

4.41 SONI requests that the UR amend Annex 1 (and the Draft Uncertainty Mechanism Guidelines) to facilitate this necessary change. The amendments should ensure that future actual costs remunerated as part of the Dt uncertainty mechanism will be approved, and allowances adjusted, as required, insofar as the costs incurred remain under the maximum (total) capped allowance.

4.42 In conclusion, we consider that the current drafting is an error and request that paragraph 2.2(i) (i) (B) is revised. We have proposed an amendment to section 2) and suggested the following additional section 3) to rectify the issue. See below.

Paragraph 2.2(i) (i) (B)

- 1) *where actual costs (excluding any such costs that are determined by the Authority at any time to be Demonstrably Inefficient or Wasteful Expenditure) incurred by the Licensee in*

relation to Approved Dt Costs defined at paragraph 8.8 of this annex) or change of law in Relevant Year t-2 are less than the costs allowed for Dt in Relevant Year t-2, the total of such actual costs;

- 2) *where actual costs (excluding any such costs that are determined by the Authority at any time to be Demonstrably Inefficient or Wasteful Expenditure) incurred by the Licensee in relation to Approved Dt Costs and change of law in Relevant Year t-2 are greater than the costs allowed for Dt in Relevant Year t-2, but within the scope of total allowances for Dt across all anticipated years, the total of such actual costs;*
- 3) *where actual costs (excluding any such costs that are determined by the Authority at any time to be Demonstrably Inefficient or Wasteful Expenditure) incurred by the Licensee in relation to Approved Dt Costs and change of law in Relevant Year t-2 are greater than the costs allowed for Dt in Relevant Year t-2, and where the total allowance for Dt across all anticipated years has been exceeded, the total of such actual costs up to the amount that the total approved amount for Dt is not exceeded.*

Paragraph 2.2 (j) The Supplemental Revenue Amount (Nt)

4.43 SONI has concerns in relation to the calculation of the ARAt term in this formula. These are discussed in full in **Key Issue 4: Hard Coded and Understated Value for Asymmetric Risk Premium (ARAt)**. SONI considers that this section will need to be updated, as discussed.

Paragraph 2.2 (k) The Remuneration of the Buildings RAB and the Non-Buildings RAB (BNBt)

4.44 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.2 (l) The Transmission Network Pre-Construction Project Amount (PCRt)

4.45 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.2 (m)- The Abandoned Transmission Network Pre-Construction Project Amount (AB_PCt)

4.46 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.2 (n) - The Remuneration of the Special Project RAB (Zt)

4.47 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.2 (o) - The Contribution from Connection Charges Income (CI0t)

4.48 SONI notes that the relevant published charging statements would need to be updated to include these costs before this term could be used. This is to ensure the various revenue line items are cost reflective.

Paragraph 2.3 (a) - The Buildings and Non-buildings Regulated Asset Bases (RAB_R)

4.49 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.3 (b) - The Weighted Average Cost of Capital (WACct)

4.50 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.3 (c) - The Opening Asset Value (ORAB_Rt)

4.51 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.3 (c) - The Closing Asset Value (CRAB_Rt)

4.52 SONI has a number of concerns under this section:

- 1) References to the Price Control Decision Paper (BC_Rt and UC_Rt)
- 2) References to the Price Control Decision Paper (CSC_Rt)
- 3) References to the Cost Categories and the Price Control Decision Paper (AC_Rt)
- 4) Link from Table E to the Allowances in the Final Determination
- 5) Limitations of AC_Rt Definition
- 6) Extent of terms included under AC_Rt
- 7) Manifestly Unreasonable drafting

Each of these are discussed below.

References to the Price Control Decision Paper (BC_Rt and UC_Rt)

4.53 SONI considers that the ex-ante allowances for BC_Rt and UC_Rt are clearly stated in Table E. Therefore, the reference to the 'Price Control Decision Paper' is unnecessary and should be removed.

References to the Price Control Decision Paper (CSC_Rt)

- 4.54 Also, under the CSC_Rt definition, there is reference to ‘... that is designed – in accordance with the principles and subject to the conditions set out in the Price Control Decision Paper – ...’. SONI failed to find any references to the ‘principles and subject to the conditions’ relating to the cost sharing arrangements (CSC_Rt) in the main Price Control Decision Paper or Annex 3. The majority of references relate to the conditional cost sharing arrangements (CSCA_Rt), which has draft guidance that the UR is consulting on as part of the Final Determination publication.
- 4.55 To avoid ambiguity and to ensure the Final Determination is codified in the licence, SONI considers that the licence should detail the ‘*principles*’ and ‘*conditions*’ associated with the CSC_Rt term. The reference to the Price Control Decision Paper should be removed. This will ensure the treatment is transparent and predictable.

References to Cost Categories and the Price Control Decision Paper (AC_Rt)

- 4.56 SONI considers the following drafting for sub paragraphs a) and i) to be incorrect and confusing:
- insofar as these costs do not fall within any cost categories for the Licensee’s overheads or support functions that are covered by the ex-ante allowance determined in the Price Control Decision Paper;*
- 4.57 SONI failed to find any reference in the Final Determination to the term ‘*cost categories for the Licensee’s overheads or support functions*’. SONI considers that the licence drafting should be clear in terms of the intended treatment of costs and the specific categories that these costs may fall into.
- 4.58 The current wording suggests that any costs relating to overheads or support functions cannot be assigned to transmission networks planning activities or connection charges. We consider this is not the URs intention and we seek clarity on the intended treatment of costs.

Link from Table E to the Allowances in the Final Determination

- 4.59 Whilst the terms BC_Rt and UC_Rt are understood, SONI is concerned that there is insufficient transparency as the figures in table E in Annex 1 are not directly presented in the Final Determination.
- 4.60 The Reasons & Effects table does not reference specific narrative in the Final Determination and does not cover how the allowances stated are derived in terms of the allowances for the non-building RAB as oppose to the Buildings RAB. In the interests of transparency, SONI considers that the UR should publish a reconciliation between Table E and the tables included in the Final Determination.

Limitations of AC_{Rt} Definition:

- 4.61 AC_{Rt} is currently defined as: the Capital Expenditure incurred in Relevant Year t by the Licensee which is reasonably attributable to RAB_R insofar as the expenditure is incurred in the performance of its activities that are authorised by or subject to obligations under the Licence, and excluding all Capital Expenditure which forms part of ...'
- 4.62 SONI has many obligations that are created outside the licence framework and that are not transposed in to it because they apply by automatic application of the law. For further information see **Key issue 12: AOT Definition and AC_{Rt} Definition.**

Extent of terms included under AC_{Rt}

- 4.63 Under the term AC_{Rt}, SONI considers that the following terms could be removed as these are not related to Capex.
- System Support Services (b)
 - Transmission Owner Business Payments (c)
 - Market Operator costs (d)
 - CAIR_t (e)
 - Pension Deficit Repairs (f)
 - Dt Costs (g)
- 4.64 SONI considers that this will ensure that the treatment of costs under the price control is clear and transparent. The current drafting introduces ambiguity.
- 4.65 In addition, SONI notes the inclusion of the wording: 'any other costs recoverable by the Licensee under the terms of the Maximum Core Revenue calculation at paragraph 2.2 above besides the BN_{Bt} term; and'. SONI has assessed each of the terms in the calculation of MC_t and does not consider that this term is required. SONI would like the UR to indicate the scenarios when this may be used. It is not included in the Reasons and Effects assessment. SONI considers that the licence should be clear on each aspect of the price control. All parties should understand how all costs are to be treated in the revenue calculations. Therefore, the use of 'catch all' terms should be avoided. SONI considers that this drafting should be removed.

Manifestly Unreasonable drafting

- 4.66 The draft licence modifications include details of actual costs which are to be adjusted to remove specific costs that sit outside the cost sharing arrangements (e.g. TNPP costs, connections). The following text has been included under sub paragraph A 2(c): '*any part of such costs which the Authority may determine from time to time to be manifestly unreasonable to include in costs which are subject to the cost sharing arrangements;*'

- 4.67 SONI is concerned that this wording overrides the DIWE calculation and may allow the UR to make any adjustments it wishes with no ability for SONI to challenge or appeal. SONI considers that the licence modifications should be such that the treatment of costs is predictable from the outset.
- 4.68 For further information see Key Issue 9: Introduction of term “Manifestly Unreasonable”.

Incorrect references

- 4.69 Paragraph 2.3 (c) (i) has been duplicated. Amendment required to include Para 2.3 (c) (ii).

Paragraph 2.4 - The Buildings RAB and Non-buildings RAB Depreciation Amount (DEP_BNBt)

- 4.70 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.5 - The Buildings RAB and Non-buildings RAB Rate of Return Amount (RET_BNBt)

- 4.71 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.6 - The Transmission Network Pre-Construction Project Amount (PCRt)

- 4.72 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.7 - The Special Project RAB Depreciation Amount (DEP_SPt)

- 4.73 SONI has no comments on the definitions in this sub paragraph.

Paragraph 2.8 - The Special Project Costs Rate of Return Amount (RET_SPt)

- 4.74 Incorrect references – Paragraph 2.7 has been duplicated. Amendment required to include Para 2.8
- 4.75 Incorrect references – Paragraph 2.8 (b) (ii) (c) 2) states Special Project X has the meaning given to it in paragraph 2.7(f). SONI considers the correct reference should be Para 2.7 (b)
- 4.76 SONI has no comments on the definitions in this sub paragraph other than the paragraph reference should be 2.8 rather than 2.7.

Paragraph 3 - Restriction of SSS/TUoS Charges: Adjustments

4.77 SONI has no comments on the definitions in this sub paragraph.

Paragraph 4 - Information to be provided to the Authority

4.78 The deletion of the term 'to the extent possible' in paragraph 4.7 (c) is not explained in the Reasons and Effects paper. It is unclear why this existing text has been removed. SONI notes that the timing of the three month statement is such that the audit for the regulatory accounts is not completed. SONI therefore cannot adhere to the latest drafting due to the timing of the reporting requirements. SONI therefore requests that the wording '*to the extent possible*' in reinstated.

Paragraph 5 - Duration of SSS/TUoS Charge Restriction Condition

4.79 SONI has no comments on the definitions in this sub paragraph.

Paragraph 6 - Change of Law

4.80 SONI has noticed that some text in this section of Annex 1 refers to out of date legislation and projects that have been delivered many years ago. This legacy text is contained in paragraph 6.3. While we are aware that this cannot be updated as part of the present exercise, without a repeat consultation, we suggest that this paragraph is reviewed and updated as part of a future consultation, for example, alongside any changes necessary to support the delivery of the new Energy Strategy for Northern Ireland. SONI will be happy to work with the UR to identify the text that requires updating and refreshed to ensure the Annex remains contemporary.

Paragraph 7 - Unit Coverage

4.81 SONI notes that the wording in Paragraph 7.3 includes a reference to Condition 30 Paragraph 6. SONI considers that this reference is incorrect and should be updated to reflect Condition 30 Paragraph 7.

Paragraph 8 - Additional Approved Costs

4.82 SONI has a number of concerns under this section:

- 1) Paragraph 8.1 - Removal of ENTSOE Membership and RSCI Costs

- 2) Paragraph 8.1 – References to out of date legislation
- 3) Paragraph 8.2 – Reference to Price Control Decision Paper
- 4) Paragraph 8.4 – Application of De Minimis Threshold
- 5) Paragraph 8.6 & 8.7 – Selection of Uncertainty Mechanisms
- 6) Paragraph 8.6 & 8.7 – Recognition of Provisional decision prior to Determination
- 7) Paragraph 8.8 to 8.11 – Confirmation of continuation of allowances beyond the end of the price control period.
- 8) Paragraph 8.8 to 8.11 - Capex and Opex references in each Uncertainty Mechanism
- 9) Paragraph 8.8 & 8.9 – Incorrect References

Paragraph 8.1 - Removal of ENTSOE Membership and RSCI Costs

- 4.83 SONI notes that the text relating to 'ENTSOE Membership' and 'RSCI Costs' has been deleted.
- 4.84 SONI notes that these cost areas are now included as allowances under the Mechanistic Cost Sharing Arrangement. This means that SONI will need to fund 25% of any increase in these costs.
- 4.85 SONI has no control over these costs and we expect these costs to increase as the number of services that SONI is mandated to obtain increase.
- 4.86 For further information please see Key Issue 2: ENTSOE membership & CORESO Allowances.

Paragraph 8.1 – References to Requirements and Guidance on Additional Approved Costs.

- 4.87 Upon reviewing this section, SONI noticed that it makes reference to the Requirements and Guidance on Additional Approved Costs. This does not align with the definitions provided and as such should make reference to the Requirements and Guidance on Uncertainty Mechanisms.

Paragraph 8.1 – References to out of date legislation

- 4.88 When reviewing this section, SONI noticed that some text refers to out of date legislation and projects that have been delivered many years ago such as the I-SEM implementation. While we are aware that these cannot be updated as part of the present exercise, without a repeat consultation, we suggest that these paragraphs are reviewed and updated as part of a future consultation for example alongside any changes necessary to support the delivery

of the new Energy Strategy for Northern Ireland. SONI will be happy to work with the UR to identify the text that requires update and refresh to ensure the Annex remains contemporary.

Paragraph 8.2 - Reference to Price Control Decision Paper

4.89 SONI considers that the highlighted text should be removed from this definition:

'In making any claim pursuant to paragraph 8.1, the Licensee shall ensure that: (a) it takes account of, and gives regard to, the Price Control Decision Paper'

4.90 The Uncertainty Mechanism Guidance Document should stand alone and be such that the Uncertainty mechanisms are predictable and clear in terms of implementation. The UR has awarded itself the ability to update the guidance and therefore the reference back to the Price Control Decision Paper is not required.

4.91 In addition, the Price Control Decision paper references out to the draft uncertainty mechanism guidance and therefore we consider that the Final Determination is not an appropriate reference. As a point of principle, the guidance should reflect the final position having considered all responses to the consultation document.

Paragraph 8.4 – Application of De Minimis Threshold

4.92 SONI welcomes the additional drafting in relation to the treatment of opex associated with Capex submissions via the uncertainty mechanisms. However, the current drafting states *'the Authority may choose not to apply the de minimis threshold to these opex costs'*. SONI disagrees with this approach as it does not provide certainty in relation to how the UR should treat submissions of this nature. SONI requests that a more definitive statement is included.

4.93 In addition, SONI is concerned about the inclusion of the 'in each Relevant Year' in this paragraph. SONI considers that the purpose of the de minimis clause is to prevent SONI from submitting smaller value items via the uncertainty mechanisms. The inclusion of 'each relevant year' may cause an incorrect treatment of allowances that fall across regulatory years (e.g. due to project phasing).

4.94 For example, SONI may submit a project at a cost of £78K where the costs occur evenly across two regulatory years. Under the current drafting, this would result in a full disallowance (£39K in each regulatory year which is below the de minimis). SONI considers that each claim submitted should be considered in its entirety and not on the phasing of when costs are incurred. This can be achieved by removing the reference to 'in each Relevant Year' from this paragraph. The current treatment will create a perverse incentive to delay the submission of funding requests to avoid being penalised for phasing issues. This is not in the interests of customers.

Paragraph 8.6 & 8.7 – Selection of Uncertainty Mechanisms

- 4.95 Under 8.6 and 8.7, the current drafting allows for the UR to determine which of the four uncertainty mechanisms will be used for approval and the option of using a combination of the mechanisms.
- 4.96 SONI seeks clarification on the criteria the UR will use in making this decision. The licence modifications are silent on the risk profile being applied when SONI make a submission. This is a significant concern for SONI.
- 4.97 For further information please see Key Issue 3.1: Limited ability to use the uncertainty mechanisms and impact on Asymmetric Risk allowance. Selection of Uncertainty Mechanism for Additional Approved Costs

Paragraph 8.6 & 8.7 – Recognition of Provisional decision prior to Determination

- 4.98 SONI notes that the UR has recently introduced a process whereby it makes a provisional decision which it shares with SONI and allows SONI to respond before a determination is made and published. SONI welcomes this new approach and considers that this step should be captured in paragraph 8.6 or 8.7 to ensure the process is transparent and understood by all parties.

Paragraph 8.8 to 8.11 – Confirmation of continuation of allowances beyond the end of the price control period.

- 4.99 SONI requests that the UR provides assurances, through additional narrative within these sections of the Annex, clarifying the treatment of approved allowances for projects anticipated to run beyond the end of this price control period. It is important that the UR provides certainty that allowances and expenditure for these approved projects will be treated in an identical manner in the period following 2024/25 until the projects are completed.

Paragraph 8.8 to 8.11 - Capex and Opex references in each Uncertainty Mechanism

- 4.100 Under 8.8 (a): Dt is defined as 'the Authority shall determine the scope of costs relating to the claim that shall be recoverable under the Dt uncertainty mechanism (e.g. by reference to specific projects or activities, by reference to cost categories such as operating expenses or capitalised expenditure, and/or by reference to periods of time).
- 4.101 In addition, under 8.9 (a): Zt is defined as per the Dt wording above as is the Et definition at 8.10 (a): and the Vt term at 8.11 (a).
- 4.102 Based on the formulae throughout Annex 1, Dt and Et appear to be treated as Opex and Vt and Zt as Capex. However, the definitions states that each term can be Capex or Opex. Clarification is required on each term to ensure they are treated correctly via the formulae.

The current drafting is silent on what happens in the scenario where the UR determines that a Dt is Capex or a Vt is Opex.

4.103 SONI considered this issue is easily resolved by defining Dt and Et as Opex only terms and Vt and Zt as Capex only terms.

Paragraph 8.8 & 8.9 – Incorrect References

4.104 SONI has noted two references that we consider are not correct:

4.105 Under Paragraph 8.8 sub para (d), there is a reference to 2.2.(i) (i) C. This sub clause does not exist. SONI considers the correct reference should be 2.2.(i) (i) B.

4.106 Under Paragraph 8.9 sub para (e), there is a reference to 2.8 (b) (ii) (C) 1) a). This sub clause within Para 2.8 does not exist as Para 2.7 was duplicated.

Paragraph 9 – Not Used

4.107 SONI proposes that this section is removed and the following section renumbered.

Paragraph 10 - Approval of Transmission Network Pre-construction Projects and Costs

4.108 SONI has no comments on the definitions in this sub paragraph.

Paragraph 11 - Reporting

4.109 SONI has no comments on the definitions in this sub paragraph.