



# SONI TSO Governance: Decision on modifications to the SONI TSO licence

30 August 2022



## About the Utility Regulator

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

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

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

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



### Our mission

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



### Our vision

To ensure value and sustainability in energy and water.



### Our values

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

## Abstract

This document sets out our decision to implement modifications to the SONI TSO licence. These changes are required to give effect to our conclusions on the changes that are needed to SONI TSO's governance structures following review by the Utility Regulator (UR). The changes will ensure more effective SONI TSO governance to the benefit of NI consumers.

This decision paper is a response to a statutory consultation on licence changes proposed to SONI TSO's licence, published in January 2022. The proposals in the statutory consultation built upon the prior work of UR's review of SONI TSO's governance, and were developed through consultation with industry and wider stakeholders.

This document outlines our reasoning for our decisions to implement modifications to the licence conditions, including how responses received to the statutory consultation have been taken into account.

## Audience

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

## Consumer impact

Compared to SONI TSO's current governance, the governance changes UR proposes to implement by means of licence modification, are designed to better secure the protection of the interests of Northern Ireland consumers and other stakeholders now and into the future.

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# Executive Summary

## Introduction

SONI Ltd is the electricity Transmission System Operator (TSO) for Northern Ireland (NI). As TSO, SONI has a central and critical role to play within the electricity sector, in particular at the present time as we are moving toward a low carbon future. It is essential that SONI is capable of discharging its TSO obligations in NI independently and in the best interests of NI consumers. It is also essential that it is clearly seen to be acting in this manner, in a way that ensures that it is fully accountable to regulators, government and (ultimately) to the NI consumers who fund its activities. SONI TSO's roles include:

- **Generation Despatch:** This “despatch” is determining adjustments to the real time output required from controllable electricity generation plant to match electricity demand, and instructing those generators accordingly. This “despatch” needs to maintain the reliability and quality of electricity supplies in an economic manner.
- **Plan Developments:** Plan the development to the NI electricity transmission system that may be required to avoid constraints that lead to un-economic curtailment of the energy production of electricity generators (where there is insufficient transmission capacity to transport that energy to where it is needed).
- **Information for Investors:** Publish information giving SONI's best view on a number of factors that are key to the investment case for new electricity plant (e.g. generation, batteries etc.) – including:
  - Planned developments to the transmission network;
  - Planned commissioning of new, and decommissioning of old, electricity plant; and
  - Analysis of the future need for electricity generation.
- **Manage Technical Standards:** Manage and monitor technical standards for the operation of the NI electricity system, including technical requirements for plant connected to that system.

SONI is owned by EirGrid plc, which is also the TSO in the Republic of Ireland. However, the corporate parent/subsidiary relationship between EirGrid and SONI must not be allowed to obscure the fact that it is SONI which is and remains accountable for making the key decisions and delivering the outputs which are required of it in its role as NI TSO. Regardless of its ultimate ownership, SONI must be independent and responsible for its choices and its performance. The manner of its decision-making must be fully transparent so that it is open to regulatory scrutiny and can be held accountable to consumers in NI.

This is the first review of SONI TSO's governance arrangements. The review was signalled during the implementation process for ISEM which confirmed that UR

would review the governance of SONI to ensure that it continues to adequately fulfil the requirements of an independent TSO for NI.<sup>1</sup>

The review was initiated in 2019 with a Call for Evidence, followed by a consultation in April 2021 on four options for changes to SONI TSO's governance arrangements. There followed a further consultation in January 2022 on potential modifications to the conditions of the SONI TSO licence. The responses to the January 2022 licence modification consultation are summarised in section 4 and in Annexes 3 and 4 of this document.

The governance review is timely, in particular because the transition to low-carbon forms of electricity generation and important changes in the use of electricity (e.g. the increase of electric vehicles and developments in battery technology) is rapidly changing the way that the electricity system operates. This in turn leads to a need to reform regulations for the electricity sector as well as the practices of the TSO. Since the TSO has a central role to play in ensuring a successful transition, it is essential that its governance and management structures command public confidence and are fit for purpose in dealing with the challenges ahead.

The electricity sector is now facing significant challenges associated with the move to low-carbon forms of generation – in particular, the change in the generation mix is progressively increasing the challenge of operating the electricity system in a stable and secure manner. These challenges are being observed across Europe, but are more extreme for the electricity system on the island of Ireland – reflecting its small size, and the nature of its electrical connections to neighbouring systems. As TSO, SONI has first-hand experience of the emerging challenges of operating a low-carbon electricity system. This experience is invaluable for the purpose of informing the development of policy to enable further decarbonisation of the sector. SONI is uniquely positioned to understand the challenges arising from the transition, and to contribute to the development of solutions to these challenges, not least in terms of:

- The types of technology that will need to be connected to the Transmission System for it to continue to operate in a stable and reliable manner;
- The approaches and systems used by the TSO for the despatch of plant (e.g. generators, batteries etc.) on the electricity system; and
- The technical standards for operation of, and connection to, the electricity system.

The adoption of these solutions will require revisions to energy policy and regulation for NI, so that SONI will be expected to work alongside UR and the NI Government as a close and trusted partner. This has similarly been recognised in Great Britain (GB), with BEIS and OFGEM jointly committing to enhance the visible independence and change the governance of the GB Electricity System Operator (ESO) so that it can best fulfil this trusted and quasi-governmental role. The Energy Bill currently before the Westminster Parliament makes provision for the ESO to be established as

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<sup>1</sup> SEM-16-041 Mitigation measures for potential conflicts of interest in the EirGrid Group

the new 'independent system operator and planner', with explicit duties to protect the interests of GB consumers, so that it is fit for the purpose of playing a key role in the low-carbon transition.

It is in this context that SONI's governance structures must be improved and brought up to date to enable it to contribute fully to the development and implementation of NI government policy in a way that is focused on the needs of NI consumers and the objectives set out SONI's TSO licence conditions. There must be no risk that SONI might be, or be perceived to be, directed or unduly influenced by EirGrid in its pursuit of its objectives and policy of government in the Republic of Ireland.

### **Purpose of this document**

This document sets out our decision to implement modifications to the SONI's TSO licence following the conclusion of UR's review of the governance of SONI TSO. It includes the text of:

- The final licence modifications we are making following consultation (see Annex 1); and
- The statutory notice of our decision to modify the conditions of the SONI TSO licence in accordance with Article 14(8) of the Electricity (Northern Ireland) Order 1992 (Annex 2).

### **Vision for SONI TSO**

Our vision for SONI is that it is a strong and effective TSO that works on behalf of and advocates the interests of NI consumers, in particular with regard to the important changes necessary on the journey to a low-carbon system. In the all-island arrangements it should work co-operatively and as an equal partner with EirGrid TSO.

We wish to make possible the realisation of appropriate synergies and efficiencies that may arise from SONI's position as part of the overall EirGrid Group, but only to the extent compatible with the overriding vision for SONI TSO.

This vision cannot be achieved if SONI's integration into the EirGrid Group is so extensive that it compromises the necessary independence that SONI must maintain within the Group, undermining the specific protections for NI consumers that SONI should deliver through the fulfilment of its TSO licence obligations.

### **Key findings from the governance review**

Our governance review has clarified the nature of SONI's current governance arrangements and the extremely limited level of autonomy the company has in its relationship with EirGrid plc. At present, SONI is integrated into EirGrid Group structures to the extent that:

- The authority and independence of the SONI Board is extremely limited as evidenced by the fact that all SONI Ltd Board members are appointed by and



on behalf of EirGrid plc (being either members of the EirGrid plc Board or of its staff) and the matters reserved to the SONI Board are very limited.<sup>2</sup>

- SONI does not have a comprehensive dedicated management team or staff to support its Board and cover the full range of TSO functions. It has only a small number of dedicated management staff.
- SONI TSO staff are pooled across the Group with management and decision making in respect of SONI TSO activities delivered under an integrated management and resource model rather than managed and controlled by SONI itself. Instead the Executive Committee of EirGrid has management responsibility for all SONI TSO licence activities as managers in the integrated structure ultimately report to the EirGrid Group CEO who in turn reports directly into the EirGrid plc Board.
- In the context of the integrated model, key protections for NI consumers are either missing or not working as intended, such as a service level agreement in relation to shared staff.<sup>3</sup>
- There is a lack of transparency to UR and NI stakeholders in key areas, e.g. over costs that are shared with EirGrid and decision making within EirGrid structures that impacts on SONI and the delivery of SONI TSO licence obligations.<sup>4</sup>
- There is no robust set of rules to govern collaboration between the TSOs for SEM purposes – these have been 'internalised' within the integrated EirGrid Group structures.

As a consequence, management and oversight of SONI TSO licence responsibilities are effectively discharged by EirGrid plc and not by SONI Ltd.

EirGrid Group decision making structures have the effect of creating a 'black box', resulting in a lack of transparency as to how decisions are made on SONI TSO functions or how the value or cost to NI consumers from decisions is taken into account. This 'black-box' makes the information asymmetry which always exists between UR and SONI considerably worse, preventing an appropriate level of transparency and limiting UR's ability to regulate SONI effectively to the benefit of NI consumers.<sup>5</sup>

Our findings from the review echo repeated stakeholder concerns about diminished transparency and accountability in SONI which were expressed in responses from consultees during the governance review.

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<sup>2</sup> See Annex 2 of the April 2021 consultation Paper for the list of matters reserved to the SONI Board.

<sup>3</sup> See Paragraph 3.21 of the April 2021 Consultation Paper for a list of key protections we consider are either missing or not working as intended.

<sup>4</sup> For further explanation see Paragraphs 2.42 and 2.43 below.

<sup>5</sup> Information asymmetry being a feature of the typical regulatory relationship between a regulator and a regulated entity.

## Potential harm for NI consumers

We consider that the present arrangements pose a number of risks for NI consumers as they:

1. **Impede UR's ability to regulate effectively.** This is due to:
  - A lack of transparency in relation to costs and how decisions are made;
  - Reduced accountability by SONI for delivery of its licence obligations arising from how SONI has been integrated into the EirGrid Group.
2. **Impede the effective performance of TSO functions in the SEM.** SONI's loss of independence has undermined both its ability to 'act in conjunction' with EirGrid for SEM purposes and the effectiveness of the rules to govern TSO collaboration in the System Operator Agreement (SOA). Consequently, we consider that there may well be an existing and ongoing breach of the SONI TSO licence conditions which underpin the interaction of SONI and EirGrid TSOs for SEM purposes.
3. **Create risks of harm to NI consumers** from:
  - Potential for inappropriately higher prices for NI consumers, particularly through the obfuscation of information (for instance that relevant to costs attribution between the TSOs) or limited incentives to challenge costs;
  - Misalignment of NI Policy and the SONI approach to network development through a 'one-size fits all' approach of a shared management model whereby investment and operating decision-making is potentially agreed in a shared management model. This includes the risk that NI network and user differences are not sufficiently represented or taken into account within decision-making; and
  - Barriers to competition whereby, again, the shared management and operating model employed across EirGrid and SONI risks a 'one-size fits all approach' which may not properly account for differences in developing and operating the NI network both in procurement of system services and system analysis and planning.
4. **Lack of independence in SONI impacts** the extent to which SONI's opinion and analysis (and not that of EirGrid) can inform the development of NI policy required to support move towards a lower Carbon electricity sector.

Several options to address these risks and ensure accountability and transparency

have been developed and refined by UR through consultation during the course of the governance review.

No evidence of actual existing harm arising from the present arrangements have come to light during the governance review. The 'black-box' nature of decision-making and the information asymmetry which exists between UR and SONI makes this difficult to establish. Be that as it may, real life examples of how the UR, in its regulation of the SONI TSO, has encountered difficulties due to an absence of transparency can be found in Annex 7.

In any case, UR does not need to evidence harm that has already occurred before it can act. It is appropriate as a matter of good regulatory practice to take proactive measures to manage and reduce the clear risks of future harm, rather than waiting until actual harm has occurred. This is also the approach taken by GB Government and OFGEM in committing to changes to the governance of the GB ESO. This entails a proactive and future-facing decision by GB Government and OFGEM to enhance the ability to transition towards a net-zero carbon future, rather than a reaction to proven harm arising from the existing arrangements.

### **Licence modifications required**

We recognise that UR does have the means to address at least some of the current information deficiencies. However, such an approach would inevitably require UR to become increasingly intrusive in its regulation of SONI. It is almost inevitable that a more intrusive approach would lead to tension between the respective roles and responsibilities of SONI and UR.

Instead we consider that licence modifications to change the governance of SONI are a better way forward, so far as they are designed to increase the accountability and transparency of SONI for the delivery of its TSO obligations, particularly at the level of the SONI Board. In turn this will foster a more trusted relationship between SONI, UR and SONI's other stakeholders.

The modifications to the conditions of SONI's TSO licence are designed to mitigate the risks identified, enhance the independence of SONI, improve the transparency and accountability of the company through better governance and management, and ultimately ensure the interests of NI consumers are protected while SONI remains a subsidiary of EirGrid plc.

The new Condition 42 to be introduced to the SONI Transmission Licence contains licence requirements in the following areas:<sup>6</sup>

- **SONI board composition and functions:** the new licence requirements follow good practice in corporate governance. They include the appointment of a new SONI board by 1 June 2023 composed of a majority of Sufficiently Independent Directors (SIDs), a definition of SID, and new requirements as to essential board member skill sets, a minimum specification of matters for which the Board must be responsible, and the terms of appointment for SIDs.

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<sup>6</sup> See section 4 of this document for a more complete summary of the licence modifications.

- **Managerial and operational independence:** the SONI TSO business is required as a starting point to be managerially and operationally separate from EirGrid and any other company within the EirGrid Group.
- **Initial derogations:** the TSO business may be exempted from the requirement that the SONI TSO business is to be managerially and operationally separate from EirGrid in respect of those business functions for which it has been given a derogation by UR. SONI may apply for derogations between 1 October and 30 November 2023.
- **Subsequent derogations: in recognition of the fact that things may change,** SONI may also apply for a derogation at a later stage, i.e. after 1 December 2028.
- **Facilitating and monitoring compliance:** the submission of a compliance plan designed to ensure compliance with Condition 42 and the appointment of a Compliance Manager to oversee its effective implementation.

In order to achieve our vision of good governance, the licence conditions balance the need for SONI to have independence from EirGrid plc with the ability to retain some measure of operational and management integration with EirGrid plc to the extent that this has been assessed by UR as demonstrably beneficial for NI consumers. The independence of the SONI Board and the derogation process are both key to our vision for good governance.

The new independent SONI Board will need as one of its first actions to decide the extent of derogations to apply for from the requirement for full separation. The Board will have the opportunity to identify those functions, systems and processes that it believes need to be integrated with those of EirGrid plc to support the SEM, or that the Board wishes to remain integrated for other reasons that add value to NI consumers. We anticipate that the SONI Board may seek derogations for a number of business functions on the basis that it considers this would be in the best interests of NI customers (e.g. because there are economies of scale and scope to be captured).

The fact that the derogation process requires the independent SONI Board to evaluate the most efficient means of delivering its licence obligations will begin to build a culture of accountability in SONI. The derogation process will also increase transparency, as it requires that a fully evidenced case will need to be made by SONI for any derogation from the separation requirements. UR remains fully open-minded as to the extent of the potential future derogations, but the onus will clearly be on SONI to prove why they should be given.

Also, in granting a derogation UR (or, in appropriate cases, its SEM Committee) has the ability under new Condition 42 to place conditions on the derogation given. The ability to place conditions will be an important regulatory tool to maintain independent SONI decision making and accountability, and in particular to ensure that SONI

implements mechanisms which open up the ‘black-box’ in circumstances where a derogation allows SONI TSO functions to remain integrated with those of EirGrid plc. In the context of the SEM the licence changes will restore an appropriate level of independence to SONI, which will allow it to act in conjunction and co-operation with EirGrid TSO and to participate in SOA structures in the manner that was always intended under the licence. This will facilitate the SEM regulatory framework to work as it was originally designed to do, and in the manner that still remains the best way of functioning.

Greater TSO independence will also support SONI in focusing on and articulating the interests of NI consumers, thereby ensuring a much greater alignment between the shareholder and NI consumer objectives. In turn this will drive increased trust and confidence of stakeholders in the development, operation and management of the NI transmission network, including in particular in respect of the changes that will need to be made as part of the transition to a low-carbon economy.

### **Costs and benefits**

The new licence condition will increase accountability, transparency, and trust in SONI to the benefit of NI consumers. Further potential benefits under the new arrangements may arise from a) challenge or rejection of Group costs by SONI; b) removal of ‘one-size-fits-all’ approach; and c) distinct service needs being developed by SONI. These benefits cannot be reliably quantified at the present time, but are expected to be material.

We acknowledge that there will be implementation and ongoing costs associated with the new SONI board and these are estimated in UR’s CBA.<sup>7</sup> Additional costs may be incurred as a consequence of the derogation process, e.g. where a derogation is sought but not granted or alternative conditions are imposed. These future costs cannot and will not be known until the derogation process has been undertaken. It is therefore not possible to make an estimate of them at this stage. UR has carefully considered the potential costs and benefits of the incorporation into SONI’s TSO licence of the new Condition, assessing them in the light of its principal objective and general duties under Article 12 of the Energy (Northern Ireland) Order 2003. It is satisfied that the decision to modify the licence conditions by introducing Condition 42 is best calculated to further its achievement of that objective and the satisfaction of those duties.

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<sup>7</sup> Costs are estimated at £348k per year, with additional cost of £50k in the first year for the establishment of the new arrangements.

# 1. Introduction

## Purpose of this document

- 1.1 This document sets out our decision to implement modifications to SONI's Transmission System Operator (TSO) licence following the conclusion of UR's review of the governance of SONI TSO. The licence changes will ensure more effective SONI TSO governance to the long-term benefit of NI consumers in fulfilment of UR's statutory duties.
- 1.2 This decision is made following a statutory consultation on licence changes to SONI TSO's licence which was published in January 2022, and fully takes into account the responses to that consultation. However, both that consultation and this decision come at the end of a much more extensive process. The proposals in the statutory consultation built upon the prior work of UR's review of SONI TSO's governance, and were developed through consultations with industry and wider stakeholders. In order to obtain the full picture of those consultations and our developing thinking, it is important to read this decision together with the documents which precede it, listed in the section below ("the Preceding Documents"). In this document we do not repeat in full the analysis which has already been extensively set out by UR in those earlier documents.

## Review of SONI TSO governance

- 1.3 In July 2019, we initiated a review of the governance arrangements of SONI to ensure that the company's governance is, and will continue to be, fit for purpose in securing the protection of the long-term interests of consumers.
- 1.4 The review was signalled during the implementation process for ISEM which confirmed that UR would review the governance of SONI to ensure that it is designed and operates in a manner that adequately satisfies the requirements of an independent TSO for NI.<sup>8</sup>
- 1.5 The review has followed these stages and milestones which are briefly recapped below and explained more fully from paragraph 1.6 below:
- a) A Call for Evidence, published on 9 July 2019<sup>9</sup>, which sought the views of all interested stakeholders as to any issues that may arise from the current SONI governance arrangements in the light of recent, and the likely future, industry developments;

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<sup>8</sup> SEM-16-041 Mitigation measures for potential conflicts of interest in the EirGrid Group

<sup>9</sup> [20190709 SONI Governance A Call for Evidence.pdf \(uregni.gov.uk\)](#)

- b) A consultation paper on 2 April 2021<sup>10</sup> which consulted on four options for potential changes to SONI TSO's governance arrangements;
- c) A statutory consultation on licence modifications to SONI's TSO licence to reflect the outcome of our governance review. The licence modifications were drafted so as to give effect to one of the options previously consulted on in April 2021 (option C).

As such the function of UR at this final stage is to decide on the licence modifications necessary to address the problems already identified, through previous consultations, in relation to SONI's governance and operational capacity/independence. In particular, this decision builds on the statutory consultation by outlining UR's key reasons for implementing the modifications on which it has now decided.

### ***Aims of the governance review***

1.6 As set out in the Call for Evidence<sup>11</sup>, when we initiated the review, the aims were to:

- Ensure SONI's TSO licence conditions on independence are clear and fit for purpose;
- Determine how SONI TSO's governance structures currently work in practice;
- Identify whether these arrangements are adequate for the future, and in particular whether they pose any risk of harm to NI consumers that requires regulatory intervention;
- Consider in particular whether additional regulatory measures (e.g. licence modifications) are needed, and if so identify and develop a proportionate regulatory response;
- Ensure that governance arrangements will remain fit for purpose having regard to the future energy transition, and do not place limits on the effective regulatory discretion of UR or the policy discretion of the UK Government and NI Executive; and,
- Ensure an outcome that is clear and transparent and secures confidence in the arrangements among market participants in NI.

### ***Call for Evidence***

<sup>10</sup> [2021-04-02 FINAL FOR PUBLICATION SONI TSO governance consultation.pdf \(uregni.gov.uk\)](#)

<sup>11</sup> See Paragraph 8.1 of the Call for Evidence.



- 1.7 The first stage of the review took the form of a Call for Evidence dated 9 July 2019 and sought the views of all interested stakeholders as to any issues that may arise from the current SONI governance arrangements in the light of recent, and the likely future, industry developments. We envisaged that the responses would assist us in identifying whether there are any issues with SONI's current governance arrangements and (if so) in understanding what steps may be needed to address them.
- 1.8 A total of 20 responses were received to the Call for Evidence, 12 of which were non-confidential and 8 of which were confidential.<sup>12</sup> Of the latter, 6 were flagged as both anonymous and confidential. The level of responses which were both confidential and anonymous was unusual and many of these responses came from SONI employees both past and present. Given the confidentiality attached to them, we did not put these responses into the public domain as stakeholders could not see and evaluate them. Nor did we rely on the content of these responses in forming subsequent proposals for consultation. However, our review of these responses suggested that they expressed concerns which were largely similar to those contained in the non-confidential responses.
- 1.9 As some of the responses suggested areas where further information could be useful, we conducted further analysis (e.g., analysis on the level of recharges between SONI and EirGrid) and sought further information from SONI to address gaps in SONI's response to the Call for Evidence.<sup>13</sup>

### ***SONI TSO governance consultation proposals – April 2021***

- 1.10 The responses to the Call for Evidence and the subsequent information request to SONI allowed us to establish how SONI's governance structures work in practice, furthering one of the aims of the governance review. We explained this more fully in section 2 and Annex 2 of the April 2021 Consultation Paper.<sup>14</sup>
- 1.11 The responses to the Call for Evidence also enabled us to identify whether SONI's governance arrangements pose any risk of harm to NI consumers. In the responses a range of stakeholder concerns were identified. Several of the observations revealed a potential, and likely an increasing potential, for harm to result from the current operating and governance arrangements, the risks of which are not sufficiently mitigated within the existing TSO licence conditions. These concerns are re-capped in brief summary in section 2 of

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<sup>12</sup> An overview of the non-confidential responses to the Call for Evidence and UR's response to these was published alongside the April 2021 consultation Paper.

<sup>13</sup> [SONI Governance Call For Evidence Responses | Utility Regulator \(uregni.gov.uk\)](https://www.uregni.gov.uk/SONI-Governance-Call-For-Evidence-Responses)

<sup>14</sup> See also section 2 of this paper for a re-cap.



this paper.<sup>15</sup>

- 1.12 We also approached the matter from first principles and assessed ‘what good looks like’ in respect of the practices, processes and behaviours we would expect of an independent TSO – in particular, what standards of transparency and accountability we should rightly expect. This is encapsulated in our vision for good governance of SONI TSO.<sup>16</sup>
- 1.13 Alongside our consideration of responses, we also considered other sources of standard-setting and good practice in corporate governance, to assess what might be learned from them as to the standards of transparency and accountability being applied elsewhere. These included relevant initiatives adopted by other regulators and the principles of the UK Corporate Governance Code (UKCGC).
- 1.14 Following the analysis of the information received through the Call for Evidence and all other relevant information, we concluded in April 2021 that: (a) the current governance structure of SONI TSO is inadequate to ensure the protection of the interests of NI consumers over the long-term; and (b) the continuation of the current situation poses too many future risks for those consumers.
- 1.15 In order to mitigate these risks and to ensure SONI meets our vision for good governance, we identified four options for potential regulatory intervention and subjected these to scrutiny through consultation. Each option involved some changes to SONI’s board composition, and then required different levels of management and operational independence from EirGrid plc. These options drew to some extent upon best practice initiatives employed elsewhere by regulators to remedy similar concerns. They were also designed to ensure that SONI and EirGrid can continue to deliver their SEM all-island TSO functions, thereby preserving the collaboration between the two TSOs which is fundamental to the SEM.
- 1.16 Our assessment of SONI TSO’s governance structures and the four options for change were published for consultation in April 2021.<sup>17</sup> However, provisionally at that stage, we explained that our initially preferred options were Options B and C.<sup>18</sup> We received eighteen (18) responses to this consultation of which four were marked as confidential. The non-confidential responses are published on our website.
- 1.17 We carefully considered the responses to the April 2021 consultation paper

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<sup>15</sup> See section 4 of the April 2021 Consultation Paper.

<sup>16</sup> See section 3 of the April 2021 Consultation Paper.

<sup>17</sup> [2021-04-02 FINAL FOR PUBLICATION SONI TSO governance consultation.pdf \(uregni.gov.uk\)](https://www.uregni.gov.uk/2021-04-02-FINAL-FOR-PUBLICATION-SONI-TSO-governance-consultation.pdf)

<sup>18</sup> See section 6 and 7 of the April 2021 consultation paper which explained and assessed each of the four options consulted on.

in order to finalise a policy position on changes needed to SONI TSO governance, and then considered what changes would be needed to the SONI TSO licence in order to give legal effect to the requirement for those changes.

### ***Statutory consultation on licence modifications to SONI TSO licence***

- 1.18 Consequently, in January 2022 we published our policy position on the changes needed to SONI TSO governance following the review by UR and the proposed modifications to SONI TSO's licence that we considered were likely to be necessary to give legal effect to this policy position. In the light of our analysis of the responses to the prior consultation we alighted upon Option C as our preference. The licence modifications that were published in January 2022 were therefore based on Option C as it was consulted on in April 2021<sup>19</sup>, except that they adopted two key changes to Option C as previously described. The nature of these changes and the reasons for them were fully explained in the January 2022 consultation paper.<sup>20</sup>
- 1.19 The January 2022 consultation was a statutory consultation taking place under Article 14 of the Electricity (Northern Ireland) Order 1992. We received nine responses to that statutory consultation. This document considers those responses and sets out our final decision on modifications to the SONI TSO licence consequent upon the governance review. (As explained above, much of UR's analysis in arriving at this final decision was initially developed in the Preceding Documents, which should therefore be read alongside this final decision in order to obtain a full understanding of the development of the policy and its rationale.) The non-confidential responses are published alongside this document on UR's website.<sup>21</sup>
- 1.20 The decision set out in this document is subject to a minimum 56 day statutory standstill period in accordance with Article 14(10) of the Electricity (Northern Ireland) Order 1992. The modification will therefore come into

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<sup>19</sup> See section 6 and 7 of the April 2021 consultation paper. Option C provides for a standalone SONI with an independent SONI board and independent SONI management and staff. However, Option C also provides for a derogation process which would permit sharing of resources with EirGrid with the approval of the UR. This would likely only be permitted in C where it would deliver tangible efficiencies for the NI consumer and/or result in SONI being demonstrably more effective than would otherwise be the case, whilst maintaining independent SONI decision making and accountability.

<sup>20</sup> Firstly, this option no longer has a specific licence duty on SONI in respect of Northern Ireland consumers. We consider that this is not necessary given that an independent SONI board will ultimately be responsible and accountable for compliance with the requirements of the TSO licence which are designed to ensure that delivery of Northern Ireland system operation is in the best interests of Northern Ireland consumers, and where, for SEM purposes, the SOA is designed to protect the interests of both Northern Ireland and Irish consumers. Secondly, the licence modification enables EirGrid to nominate one member of the SONI board should they wish to do so. Option C did not previously facilitate this – unlike Option B where an EirGrid appointment was explicitly a possibility.

<sup>21</sup> SONI's response includes a number of redactions at their request.

effect on 26 October 2022, unless it has first been appealed to the Competition and Markets Authority (CMA) and the CMA has both granted permission for the appeal and suspended the coming into effect of the modifications.

- 1.21 Once they are in force, the modifications must then be implemented by SONI to the timescales set out in the licence condition itself.

## 2. Importance of SONI TSO independence from EirGrid plc

### SONI TSO's role

- 2.1 SONI is the Transmission System Operator (TSO) for NI.<sup>22</sup> As such, it has a key role in the development and operation of critical infrastructure. We believe that SONI needs to have a governance structure that ensures that it is independent, transparent and accountable, and focused on delivering and protecting the needs of NI consumers.
- 2.2 As TSO, SONI has general duties under the industry legislation to:
- Ensure the development and maintenance of an efficient, co-ordinated and economical system of electricity transmission;
  - Contribute to security of supply through adequate transmission capacity and system reliability; and
  - Facilitate competition in the supply and generation of electricity.
- 2.3 SONI's licence obliges additionally it to undertake a number of activities, collectively referred to as the Transmission System Operator Business, which include:
- Planning and operating, and co-ordinating and directing the flow of electricity onto and over, the transmission system;
  - Maintaining security standards;
  - Instructing adjustments to the energy output and consumption of specific plant (this is done to maintain the system energy balance in an economic manner);
  - Procuring System Support Services (including DS3 services);
  - Operating the Capacity Market.
- 2.4 SONI TSO is thus responsible for carrying out functions that are at the core of the effective, secure and efficient operation of the NI electricity system, and therefore vital to the interests of the NI economy as a whole.

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<sup>22</sup> We explained SONI's role in more detail in the Preceding Documents. See in particular, section 1 of the April 2021 Consultation Paper which explained SONI's role as TSO and SONI's role as Market Operator in the SEM (SEMO). Further background to the TSO role may be found in section 2 of the Call for Evidence. Also, section 3 of the Call for Evidence includes information on SONI's TSO licence.

- 2.5 SONI also plays a key role in the Single Electricity Market (SEM) between NI and Republic of Ireland. SEM requires certain TSO functions to be carried out jointly and on an all-island basis (such as scheduling and dispatch) by EirGrid and SONI TSOs. However, in accordance with legislation and the TSO licences held by EirGrid and SONI, each TSO only operates in its respective jurisdiction. EirGrid cannot legally operate as TSO in NI, and SONI cannot legally do so in Republic of Ireland. Consequently the TSO licences of both SONI and EirGrid require them to act in conjunction and co-operation with each other to deliver these all-island TSO functions; and for that purpose to enter into, comply with, and maintain a System Operator Agreement (SOA) which sets out how they will work together. The SOA dates from 2007.<sup>23</sup> Neither it, nor the regulatory system of which it forms part, either states or implies that the TSOs are to act as one single entity in respect of the activities that it governs.<sup>24</sup>

### **SEMO**

- 2.6 SONI holds a second licence which licenses SONI as the SEM Operator (SEMO and SEMO Licence). The SEMO Licence regulates the roles of 'Market Operator' (MO) and 'Nominated Electricity Market Operator (NEMO).'<sup>25</sup> EirGrid holds an equivalent licence in the Republic of Ireland and both are accountable to the Single Electricity Market Committee (SEMC) via their SEMO licences for discharging the MO and NEMO functions.
- 2.7 The structure and governance of the MO is a contractual joint venture between EirGrid and SONI. This requires EirGrid and SONI to work as a single team by contrast to the separate co-operation requirements imposed on them as TSOs. SEMO has its own resources separate to those of the TSOs, together with a single regulatory price control, which is distinct from the two individual TSO price controls – the SONI TSO price control in NI and the EirGrid TSO price control in Republic of Ireland. The SEMO activity is contractually underpinned by the Market Operator Agreement (MOA), but the governance structure is quite different than that of the SOA and comprises a Governing Committee and a General Manager. This reflects the truly 'single' manner in which the MO activity is undertaken by EirGrid and SONI.

## **The importance of SONI TSO independence**

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<sup>23</sup> System-Operator-Agreement.pdf (soni.ltd.uk)

<sup>24</sup> See annex 6 for more information.

<sup>25</sup> The MO role includes the administration and maintenance of the 'Single Electricity Trading and Settlement Code,' the operation and maintenance of the SEM Trading and Settlement System and acting as 'Agent of Last Resort'. The NEMO activity includes performance of the day-ahead and intraday market coupling arrangements which includes (as defined by the CACM Regulation) operation of the day ahead market and operation of the intraday market.

- 2.8 SONI TSO is licensed in NI and regulated by UR with its principal objective of protecting the interests of consumers. SONI TSO's activities are largely funded by NI consumers. As explained above it plays a critical role in the NI electricity system. It therefore must be capable of discharging its TSO obligations in NI independently.
- 2.9 There are a number of licence conditions in SONI's TSO licence that relate to the independence of the TSO and these are intended to support the TSO in meeting its wider licence obligations to the benefit of NI consumers, in particular:
- Condition 3, "Availability of Resources and Undertaking of Ultimate Controller", requires SONI to obtain an undertaking from the ultimate controller that it will refrain from any action which would be likely to cause the Licensee to breach any of its obligations.<sup>26</sup>
  - Condition 3A, "Parent Company Undertaking from EirGrid plc", requires EirGrid plc to provide an undertaking that the licensee shall have adequate financial and non-financial resources.
  - Condition 5, "Prohibition of Cross-Subsidies", requires SONI to procure that the Transmission System Operator Business gives no cross-subsidy to, and receives no cross-subsidy from, any other business of the Licensee or of any affiliate or related undertaking of the Licensee. No change was made to this condition upon the acquisition of SONI by EirGrid.
  - Condition 12, "Independence of the Transmission System Operator Business", is intended ensure the independence of SONI and separation of control of it from generation and supply interests. The policy rationale for this is primarily to ensure equitable treatment between generation companies or suppliers, which rely on access to the transmission system.
- 2.10 To the extent that SONI TSO's current governance arrangements do not ensure its full independence – and, in particular, diminish transparency and accountability in how SONI makes key decisions as TSO - this would undermine SONI's ability to comply with its licence conditions and be detrimental to NI consumer interests. It could also expose SONI to potential enforcement action for breach of its TSO licence.
- 2.11 We recognise that EirGrid plc is the parent company of SONI meaning that SONI is not a standalone company but part of the EirGrid Group. In these

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<sup>26</sup> To facilitate the acquisition by EirGrid, this provision was suspended and replaced with a provision requiring the licensee to obtain the undertaking from EirGrid.

circumstances the parent/subsidiary relationship between EirGrid and SONI must ensure that SONI is and remains accountable for compliance with the TSO's obligations (notwithstanding its ultimate ownership), and that its activities are transparent and so open to regulatory scrutiny and accountability in NI.

- 2.12 The need for an independent TSO focused on delivering and protecting the needs of NI consumers has been brought into sharp relief by the transition to a lower carbon economy.<sup>27</sup> This will bring unique challenges and SONI will have a key role to play in helping to shape the formation and in achieving the implementation of NI Government policy. The energy transition to net-zero creates a need to ensure that SONI is able to effectively achieve the NI Executive's targets in line with the interest of NI consumers in a manner which is transparent and secures accountability and consumer and market trust in SONI TSO.
- 2.13 The move to low-carbon forms of generation – including wind and solar – is progressively increasing the challenges of operating the electricity system in a stable and secure manner. These challenges are being observed across Europe but are more extreme for the NI electricity system – reflecting its small size, the location of areas suited to renewable generation compared to extant grid assets, the unique nature of the SEM, and the nature of its electrical connections to neighbouring systems.
- 2.14 As TSO, SONI is uniquely positioned to understand the operational challenges to the electricity system arising from low carbon generation, and to contribute to the development of solutions to these challenges that meet the needs of NI policy in terms of:
- The types of technology that will need to be connected to the Transmission System for it to continue to operate in a stable and reliable manner;
  - The approaches and systems used by the TSO for the despatch of plant (e.g. generators, batteries etc.) on the electricity system; and
  - The technical standards for operation of, and connection to, the electricity system.
- 2.15 The adoption of these solutions will require SONI to work alongside UR, NI Government, NIE Networks and other stakeholders as a trusted partner – bringing SONI's unique insights derived from its hands-on experience in operating the system. A lack of independence, or even a perception of such,

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<sup>27</sup> The regulatory challenges for electricity arising from moves to a Lower Carbon Economy were highlighted in section 1 of the April 2021 Consultation Paper and in section 2.5 of the same paper which explained how GB is dealing with similar challenges.



will undermine trust in SONI TSO. This has similarly been recognised in GB, with BEIS and OFGEM jointly committing to change the governance of the GB Electricity System Operator to an extent that it can fulfil this trusted role. The significance with which this matter is being treated in GB is reflected in the fact that the UK Government is bringing forward legislation – Part 4 of the Energy Bill currently before the Westminster Parliament – to create the role of 'Independent System Operator and Planner' to enhance the remit and improve the governance of the existing GB System Operator. The future-facing role of the system operator in NI is no less important than in the other parts of the UK.

- 2.16 More particularly it is important to UR and NI Government that SONI has sufficient independence to be able to acknowledge and address the difference in policies between NI and Republic of Ireland, as well as the fact that such differences are legitimate. A number of such differences that affect the TSO role already exist, and as NI policy is developed, such differences are likely to continue to increase in number and may increase in impact.<sup>28</sup>

### ***SONI TSO independence and the SEM***

- 2.17 SONI independence also underpins the regulation of the TSO activities in the SEM as it is a prerequisite for the two TSOs to work together to deliver the all-island TSO functions.<sup>29</sup>
- 2.18 Ensuring that the interests of consumers of electricity in Republic of Ireland and NI are separately articulated and then appropriately protected is a key driver for the SEM regulatory arrangements, and the 'acting in conjunction' concept which underpins the SOA is a feature of these arrangements which aim to maximise the interests of both sets of consumers. See Annex 6 for more details of the regulatory regime.
- 2.19 How the two TSOs interact for SEM purposes is critical to this outcome. Each should bring knowledge of, and speak for, the needs of the consumers in their jurisdiction in the context of the relevant network characteristics and policy framework. Cooperation, or 'acting in conjunction', under the SOA should enable SONI and EirGrid to reach conclusions which are designed to ensure that the overall outcomes from the SEM are a win-win for both sets of consumers.
- 2.20 If SONI TSO is so integrated into EirGrid Group structures that it cannot articulate and bring a NI jurisdictional perspective to TSO discussions about SEM issues, then the NI perspective may not be taken into account

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<sup>28</sup> See Annex 5.

<sup>29</sup> We explained the importance of SONI TSO independence to the SEM in more detail in the Preceding Documents. See in particular See Paragraphs 3.17-3.25 of the January Licence Modification Consultation Paper.



(sufficiently or at all) in TSO decisions resulting in sub-optimal decisions for NI consumers. The proper functioning of the SOA relies on structures, which allow any tension between jurisdictional perspectives to play out in joint TSO decision-making, and to do so in ways that are clear and open to UR (i.e. to ensure transparency) which in turn makes it possible for the quality of the decisions to be subject to appropriate regulatory scrutiny (i.e. accountability).

- 2.21 Moreover the SOA is fundamental to the ability of each regulator to enforce compliance with TSO functions in the SEM. The SOA provides SONI with a means of ensuring EirGrid does those things which SONI requires for the purposes of compliance with its regulatory obligations (and vice versa) such that, from UR's perspective, SONI is directly responsible for its licence compliance even where it relies on EirGrid to do things to support such compliance.
- 2.22 Consequently, under our vision for good governance, SONI TSO's governance structures must facilitate:
- Collaboration with EirGrid as an equal partner and on the basis of a formal agreement with clear rules;
  - The establishment and operation of mechanisms to resolve disputes between the TSOs; and
  - Decision-making which records how the balance between the interests of the two different sets of consumers had been struck, in particular where they are not aligned.
- 2.23 In the absence of two independent TSOs, working "in conjunction" with each other through a formal set of rules (at the core of which is an *operative* SOA), there is a likely breach of the SONI TSO licence conditions which underpin the interaction of SONI and EirGrid TSOs for SEM purposes.

## **Vision for SONI TSO**

- 2.24 Our vision for SONI is that it is a strong and effective TSO that works on behalf of and advocates the interests of NI consumers.<sup>30</sup> In the all-island arrangements it should work as an equal partner with EirGrid TSO. It is our aim through this review to ensure SONI TSO's governance structures are able to support this vision by underpinning the long term success and sustainability of the TSO business. Therefore SONI TSO's governance must meet the needs of, and realise the benefits for, NI consumers. Going

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<sup>30</sup> We explained our vision for good governance and our vision for SONI in more detail in the Preceding Documents. See in particular section 3 of the April Consultation Paper where we set out the vision for good governance in SONI and assessed whether SONI meets this vision.

forward, the structures need to be fit for purpose and appropriately designed and implemented so as to:

- Secure the protection of the interests of consumers and other stakeholders, including generators and suppliers, in NI;
- Allow for the implementation of NI regulatory policy, whether or not relating to SEM;
- Enable SONI to play its role in the implementation of the policy of the UK Government and/or NI Executive, and in particular to facilitate the industry's energy transition; and
- Maintain cross-jurisdictional relationships necessary to facilitate the SEM;

While also:

- To the extent compatible with the above requirements, permit the realisation of appropriate synergies and efficiencies that stem from SONI's position as part of the overall EirGrid Group.

2.25 As has been made apparent in the responses to the Call for Evidence and the other information gathered by UR in the course of its various consultations, this vision is undermined by the loss of SONI's independence within the EirGrid Group.

### **SONI TSO loss of independence within EirGrid Group**

2.26 In 2009 SONI was acquired by EirGrid<sup>31</sup>. The acquisition gave rise to concerns as to whether consumers on the island of Ireland, and particularly in NI, would continue to be protected, and would not be disadvantaged by the change in control of SONI. The concern was whether SONI would be managed purely with a view to achieving the objectives set out its own licence conditions, or whether SONI might be unduly influenced by EirGrid's pursuit of its separate corporate objectives.

2.27 Consequently a number of measures were voluntarily put in place by EirGrid, including a new obligation which was added to the EirGrid TSO licence requiring it to at all times have regard for the interests of consumers in NI as well as Republic of Ireland. However, UR does not have any powers or role in relation to the EirGrid TSO licence, and has no visibility of the

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<sup>31</sup> We explained the SONI TSO's loss of independence since acquisition by EirGrid in more detail in the Preceding Documents. See in particular section 3 and annex 2 of the April Consultation Paper. Further background information on the acquisition and the EirGrid Group structure is provided in sections 2 and 4 of the Call for Evidence.

effectiveness of these measures.

- 2.28 The governance review has revealed that, since acquisition, SONI's practical independence as a company within the EirGrid Group has been reduced very significantly – arguably, indeed, that it has been lost completely. Information provided by SONI in response to the Call for Evidence revealed that the model applicable to SONI within the EirGrid Group is highly centralised, characterised by a strong central EirGrid plc Board, a limited Board at subsidiary level (principally, or at times wholly, constituted of EirGrid Board members or employees), a range of corporate policies applicable to subsidiaries, and pooling of subsidiary resources in a shared resource model reporting upwards to the EirGrid plc Board.
- 2.29 Some loss of independence might be expected following acquisition by another corporate entity. But in the case of SONI, which is separately regulated by UR and funded by NI consumers, any loss of independence should be balanced by the maintenance of strong protections for the interests of NI consumers and not be detrimental to compliance with SONI's TSO licence obligations. We consider that the balance has tipped too far in favour of EirGrid plc, as SONI has in substance become a "business unit" within the EirGrid Group. It has no demonstrable independence of mind or action.
- 2.30 Stakeholders raised concerns with UR during the governance review about the lack of transparency and accountability in SONI since acquisition.
- 2.31 The fact that SONI has been integrated into Group structures across a range of areas over time is not driven by any SEM requirements – as explained above (and in Annex 6) the SEM requires the two TSOs to act in conjunction, collaboration and cooperation with each other, but not the institutional integration of the TSOs or the creation of a single TSO. On the contrary, full institutional integration, inevitably on the terms preferred by the parent entity, appears to run counter to the need for co-ordination between the two TSOs acting as equal partners in relation to their respective jurisdictions.
- 2.32 Substantive integration of SONI into Group structures is made possible by the fact that EirGrid carries out very similar functions to SONI, and does so alongside SONI on the all-island transmission network. This has afforded considerable scope for either TSO to carry out the functions of the other. These interactions are not necessarily those envisaged by the SOA, because in these interactions one TSO is performing functions on behalf or in place of the other rather than in conjunction with it.
- 2.33 The features of SONI's governance which limit the TSO's ability to articulate NI consumer interests and ensure these are being taken into account

include:<sup>32</sup>

- SONI Board composition and scope of responsibility;
  - Limited dedicated SONI management and staff team to support the SONI Board;
  - An integrated management structure operated across the Group;
  - In the shared resource model key protections for NI consumers either missing or not working as intended.
- 2.34 The majority of SONI Board members are either also EirGrid plc board members or are EirGrid staff. There are no non-executive directors on the Board who are independent of EirGrid plc.
- 2.35 From the information provided by SONI it is clear that the matters reserved to the SONI Board are extremely limited and that a number of significant SONI functions are discharged either by the EirGrid plc Board or within the EirGrid Group integrated management structure, and with the SONI Board having no formal role.
- 2.36 Similarly dedicated resources in SONI to support the Board are limited as SONI does not have a comprehensive dedicated management team or staff which is responsible for SONI TSO functions and which reports to the SONI Board. Instead SONI Managers and staff are pooled across the Group, ultimately reporting to the EirGrid Group CEO who in turn reports to the EirGrid plc Board. This means that the Executive Committee of EirGrid has management responsibility for all SONI TSO licence activities, including network operations, planning and company finances, and operates these through an integrated management structure. The SONI MD also reports to the Group CEO.<sup>33</sup> Grid development and investment decision-making is also undertaken by Group wide committees within the EirGrid Group integrated management structure with oversight ultimately by the EirGrid plc Board.
- 2.37 Therefore, from the information provided by SONI in response to the Call for Evidence we have concluded that neither the SONI Board, nor the SONI MD, has full and transparent oversight of the management and discharge of SONI TSO licence functions and the allocation of resources available to SONI TSO.
- 2.38 Given that SONI is separately licensed in NI, regulated by UR and funded by

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<sup>32</sup> See section 3 and annex 2 of the April 2021 Consultation Paper.

<sup>33</sup> The SONI MD is not presently a member of the EirGrid executive team diminishing the visibility of SONI in the current integrated structure. See '[Our Leadership \(eirgridgroup.com\)](http://eirgridgroup.com)' The EirGrid Group CEO is instead a member of the SONI management team. See '[Our Leadership \(soni.ltd.uk\)](http://soni.ltd.uk)'.

NI consumers, we would expect that any shared resource model across the Group would have mechanisms designed to ensure that a SONI perspective can be developed and articulated within Group structures which aligns with the needs of NI consumers in order to better protect those consumers. However, the information provided by SONI indicates that key protections for NI consumers are either missing or not working as intended. For example<sup>34</sup>:

- There is no Service Level Agreement in place between EirGrid plc and SONI Ltd., such that the SONI Board could either approve or monitor prescribed performance levels and value for money from a shared management organisation.
- The Group Cost Allocation and Recharge Policy provides the basis for cost allocation across the EirGrid Group. We have seen no evidence of a performance management or approval process in place to ensure that SONI is provided with appropriate costs and service to allow it to judge whether EirGrid is acting in a manner which protects the interests of NI consumers.
- SONI has stated that the SOA has been ‘internalised’, which for all practical purposes appears to mean that it is not being complied with as drafted and is being treated as a dead letter, contrary to the underpinning licence obligation.

2.39 As UR has explained in the Preceding Documents (and further below) it is the *potential* for harm to arise from this situation and a desire to optimise consumer benefits which makes it necessary to act. Accordingly (as further explained below), SONI’s position that there is no evidence of actual harm (for example, no evidence – on SONI’s position – of the needs of NI consumers being seen as lower priority<sup>35</sup>) is beside the point. UR’s concern is as to the risk of harm. That said, UR does consider that there are real life instances where the interests of NI consumers are being neglected or overlooked under the current governance structure. See the first example in Annex 7 which sets out some worked examples of harm to transparency and the NI interest.

2.40 Moreover, SONI and EirGrid’s response to the January 2022 Consultation (and the Preceding Documents) is significant. Neither company seeks to address the UR’s concerns by providing evidence of instances where the interests of NI consumers have been specifically considered. Nor does either company explain or even acknowledge that there is a distinct NI interest which merits consideration and requires to be given due weight. Their joint approach is that the interest of the NI consumer is by definition met by a

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<sup>34</sup> And see further in particular Paragraph 3.21 of the April 2021 Consultation.

<sup>35</sup> See for example, SONI’s response to the April 2021 Consultation at Paragraph 4.45.

shared system approach (an approach with which, for the reasons explained in the April 2021 Consultation Paper and below at section 3, we disagree).

## **Impediments to effective regulation in current arrangements**

- 2.41 SONI's limited independence from EirGrid plc impedes UR's ability to regulate the TSO effectively for a number of reasons.
- 2.42 Firstly, transparency as to how decisions are made in relation to SONI's TSO functions has been greatly reduced, and in many instances has been lost altogether. Without transparency the TSO's activities are not properly open to regulatory scrutiny, problems cannot be revealed over time and the regulator cannot take corrective action. A lack of transparency therefore limits UR's ability to regulate SONI effectively, and accordingly gives rise to a lack of proper accountability for TSO decisions. SONI is now so integrated into EirGrid's decision-making structures, this has the effect of creating a 'black box', the internal workings of which are not visible. For example:
- Restrictions in the matters reserved to SONI mean that many decisions of interest to UR are taken at the EirGrid Board. Whilst UR can request SONI board minutes, the same is not true for those of EirGrid plc.<sup>36</sup>
  - Many decisions are taken in EirGrid Group committees or these set the strategic direction on the matters within their purview. UR does not have an overview of the extent of committees that may consider matters relevant to NI, minutes are typically not published and UR cannot request EirGrid Group committee minutes. These committees are therefore particularly opaque from UR's point of view, yet they consider and determine matters of significant importance in NI. For example, from information given to UR by SONI during the governance review, it appears that decisions on the development of the NI grid are taken through various EirGrid Group committees associated with the capital planning process.<sup>37</sup> Also, the Group Operational Policy Review

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<sup>36</sup> EirGrid plc Board minutes are published but can be heavily redacted – see for example, [Board-Minutes-October-2020-redacted.pdf \(eirgridgroup.com\)](#)

<sup>37</sup> The governance review has established the role of three such Committees (see annex 2 of the April 2021 Consultation Paper):

1) the Grid Infrastructure Committee (GIPC) which determines general policy and strategy in relation to the development of the Grid, and oversee the implementation of the grid development strategies in NI and Ireland. In February 2020 SONI told us that the GIPC consists of four members of the EirGrid plc Board, with relevant Executives invited, as required,

2) the Transmission Investment Committee (TIC), the role of which is to ensure good governance in relation to network capital investment decisions and provide oversight in the monitoring and control of the network development in NI and Ireland. Managers and staff from SONI attend TIC meetings as appropriate, and



Committee (OPRC)<sup>38</sup>, governs the process of operational policy changes in EirGrid and SONI.

- Significantly, the SONI board has no formal role in either taking or approving procurement decisions which incur a cost for SONI. These decisions are taken elsewhere within the EirGrid Group.
- Day-to-day decisions, such as decisions on cost allocations to SONI and on the development of key TSO work, are also taken by managers in the integrated management structure without needing the approval of the SONI board.
- A corollary of this lack of transparency is that it is hard for UR to understand the extent to which this “black box” situation has already created an actual harm for NI consumers. As explained below and in the Preceding Documents<sup>39</sup>, the UR is deciding to act by reason of the *potential* for harm and the desire to optimise consumer outcomes. However, the first example in Annex 7 is perhaps an instance where NI interests were seemingly overlooked in SONI decision making for reasons which (absent an insight into SONI decision making) are unclear to the UR.

2.43 Secondly, transparency in relation to costs has also reduced. Costs shared with EirGrid have increased over time but UR does not have visibility over the relevant total costs (i.e. the EirGrid portion and the SONI portion). Consequently, we need SONI to be able to appropriately challenge its cost allocation, and the quality of service and value for money which this represents, and to have governance mechanisms which allow it to do so. The current governance arrangements work against this as SONI is a mere price taker under the Group recharge policy.<sup>40</sup> There is no Service Level agreement (SLA) with EirGrid, and the governance structure does not allow SONI TSO either to challenge or formally agree its allocation of costs. This was highlighted in particular the April 2021 consultation paper<sup>41</sup>, where we had found:

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3) Management infrastructure Committee (MIC) the role of which is to provide support and assurance to the TIC. Similarly, managers and staff from SONI attend MIC meetings as appropriate, depending on the jurisdiction of the projects under consideration.

<sup>38</sup> [PowerPoint Presentation \(soni.ltd.uk\)](https://www.soni.ltd.uk)

<sup>39</sup> The evidence of potential harm was set out in section 4 of the April 2021 Consultation Paper and we explained that it is not necessary for UR to identify a source of harm before it can act at page 8 of the April 2021 Consultation Paper and Paragraphs 3.67-3.68 of the January Licence Modification Consultation Paper.

<sup>40</sup> The allocation of costs to SONI TSO is either made on a “broad brush” basis (e.g. SONI TSO takes 25% of overall costs) or is based on a management assessment. Ideally, this should be more objectively linked to the actual cost of resources deployed to, or needed by, SONI TSO.

<sup>41</sup> Paragraph 3.15.

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

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

2.44 We have also observed a growth in cross-business charging between SONI and the rest of the EirGrid Group. In the course of the governance review, we conducted a further analysis of SONI’s TSO Regulatory Accounts.<sup>42</sup> The allocation of costs is made on what we consider to be a broad brush basis (i.e. SONI takes 25% of the costs), or based on a management assessment. However, due to the limited role of the SONI board in financial matters, UR is unable to have any confidence that cross-business charging is being adequately scrutinised by SONI.

2.45 UR explained that the risk of potential harm in electricity customers paying too much arises from this lack of transparency (see April 2021 Consultation at paragraph 4.10). Worked real life examples of how the UR, in its regulation of the SONI TSO, has encountered difficulties due to an absence of transparency can be found in in Annex 7.

2.46 Thirdly, independent accountability by SONI for the delivery of its TSO responsibilities has been reduced, if not eliminated entirely. We have concluded that the management and oversight of SONI TSO licence responsibilities are effectively discharged by EirGrid plc, and not by SONI Ltd. However, EirGrid plc is not licensed as a TSO in NI and is not regulated by the UR, so we cannot hold EirGrid to account. Holding SONI to account is insufficient in circumstances in which SONI does not have the power under

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<sup>42</sup> This is set out in the Proceeding Documents at Paragraph 4.10 of the April 2021 Consultation Paper and Paragraphs 4.23-4.24 of the January 2022 Licence Modification Consultation Paper.



the current governance structures to independently take many of the decisions relevant to SONI's obligations as the TSO.

- 2.47 Fourthly, the governance arrangements undermine SONI's ability to comply with its licence conditions. In turn this could be detrimental to NI consumer interests and also expose SONI to potential enforcement action for breach of its TSO licence.
- 2.48 We explained in the January 2022 Consultation at paragraphs 6.3 – 6.7 that we considered governance changes are better than more intrusive regulation in order to address these concerns by reason of the increased accountability and trust which they will generate.

### *Impediment to effective regulation of the SEM*

- 2.49 The evidence we have received indicates that a consequence of SONI's loss of independence within the Group is that there is no legally or practically effective SOA in place between EirGrid and SONI TSOs, as expressly required by the TSO Licence in Condition 24 (considered further below).<sup>43</sup> SONI states that the rules meant to govern collaboration between the two TSOs for SEM purposes have been 'internalised' by virtue of the shared management structure operating across the Group. We do not accept that such 'internalisation' fulfils the requirement of the licence condition, and indeed have concluded that it runs counter to the fulfilment of the condition. The 'acting in conjunction' principle underpins the delivery of the all-island TSO functions in the SEM. This principle does not envisage the creation of a single TSO/internalisation of TSO working arrangements, but instead two separate TSOs working jointly to deliver all-island TSO obligations on the basis of a collaboration between equals. The SOA is the contractual means to ensure that EirGrid provides whatever assistance SONI needs to fulfil SONI's all-island obligations.<sup>44</sup> The so-called 'internalisation' makes the articulation of a distinctive SONI perspective (which is to say, a perspective reflecting the interests of NI consumers) much more difficult to ensure, and obscures from external view whether and to what extent such a perspective has been given at all and to what extent (if any) it has influenced the final decision. In a fully 'internalised' structure, how any tension between jurisdictional perspectives plays out in joint TSO decision making lacks any

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<sup>43</sup> Concerns about the lack of a SOA to transparently govern collaboration between the two TSOs in the SEM were evident from responses to the Call for Evidence and the April Consultation Paper. These concerns were set against SONI's view that this agreement has been 'internalised' by the shared operating model employed across the EirGrid Group. In the Proceeding Documents Paragraphs 3.17-3.25 of the January Licence Modification Consultation explains why the SOA is central to the SEM arrangements and this is further emphasized in Annex 6 below.

<sup>44</sup> See Annex 6 for more information.

real transparency, and consequently lacks proper regulatory accountability.

- 2.50 Furthermore, even assuming such internalisation is permissible (which we think it is not) SONI's response to our enquiries has not provided any evidence which gives us comfort that the 2007 SOA as "internalised" is being implemented in practice or is effectively operational at all.<sup>45</sup> For example, SONI has been unable to demonstrate that personnel are deployed or trained to fulfil its functions, or that the necessary governance exists as the committees required in the SOA do not seem to be in place (with or without SONI representation). Nor has SONI been able to satisfy us that periodic review of the SOA has taken place. Certainly no annual reporting to UR has occurred.
- 2.51 Consequently, we are concerned that there may well be past and ongoing contraventions of a number of aspects of Condition 24 concerning the SOA, e.g.:
- Condition 24(1) which obliges SONI TSO to enter into, comply with and at all times maintain in force a System Operator Agreement (SOA), which meets the requirements of paragraphs (a) to (e) of Condition 24(1);
  - Condition 24(3) which obliges SONI to periodically review the SOA and its implementation; and
  - Condition 24(7) which obliges SONI TSO to report annually to the Authority on the operation of the SOA to the extent relevant to the functions, rights and obligations of SONI TSO.
- 2.52 We also note that there are other licence conditions which are affected by the failure to have an operational SOA. For example, Condition 27(2) requires that the SOA provide for the manner in which requests are made to the SONI TSO by the EirGrid TSO for the use of transmission networks in respect of generation in the Republic of Ireland. The SOA is required to make provision for payments in respect of such use and the allocation of costs in respect of such use (Condition 27(3)).
- 2.53 In our view licence enforcement action on its own will be insufficient to fix any potential contraventions of Condition 24 (and related licence conditions). This is for the simple reason that the SOA is meant to build upon the foundation of there being two functionally and institutionally separate TSOs

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<sup>45</sup> In order to gather further information we initiated the informal stage of our enforcement procedure in 2021 and the Article 51 Notice to which SONI refers formed part of our work in this regard.

(for all the reasons explained above and in Annex 6). Absent this starting point, meaningful compliance with the licence obligations is not feasible. Consequently, measures to address SONI's independence within the EirGrid Group are first needed in order to create the institutional basis on which the SOA and SONI's participation in the SOA structures can be meaningful and effective, and thereby secure compliance with the licence.

- 2.54 For this reason we intend to pause our investigation into the issues we have (provisionally) identified in relation to the operation (or lack thereof) of the SOA and SONI's compliance with the requirements of Condition 24 pending the implementation of licence modifications as a first and necessary step.

### *Potential risk of harm*

- 2.55 In addition to impeding effective regulation, our assessment of the current arrangements has also led UR to judge an increased risk of harm to NI consumers from<sup>46</sup>:

- **Potential for inappropriately higher prices for NI consumers**, particularly through the obfuscation of information (for instance that relevant to costs' attribution between the TSOs) or limited incentives to challenge costs;
- **Misalignment of NI Policy and the SONI approach to network development** through a 'one-size fits all' approach of a shared management model whereby investment and operating decision-making is potentially agreed in a shared management model. This includes the risk that NI network and user differences are not sufficiently encapsulated within decision-making; and
- **Barriers to competition** whereby, again, the shared management and operating model employed across EirGrid and SONI risks a 'one-size fits all approach' which may not properly account for differences in developing and operating the NI network both in procurement of system services and system analysis and planning.

- 2.56 The potential for harm was discussed extensively in the April 2021 consultation paper (section 4).

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<sup>46</sup> We explained the potential risk of harm in the Preceding Documents. Section 4 of the April 2021 Consultation Paper considered the evidence received in the responses to the Call for Evidence and assessed whether actual or potential harm exists to electricity consumers in NI as a result of SONI's current governance arrangements. We then considered whether the risk of harm we had identified could be mitigated by existing provisions for the regulation of SONI. We also identified several areas of concern which were not sufficiently mitigated within the TSO Licence - see section 5 of the April 2021 Consultation Paper.

## Condition 42 a proportionate and flexible solution

2.57 UR has concluded that it needs to act in order to<sup>47</sup>:

- Ensure that it can regulate SONI effectively;
- Ensure the effective participation of SONI TSO in the SEM structures;
- Proactively take measures to manage and reduce the risks of harm to NI consumers identified, rather than waiting until there is firm evidence that actual harm has already occurred; and
- Address the underlying causes which give rise to potential ongoing licence breach of its TSO licence conditions by SONI (e.g. those that require SONI TSO to act in conjunction with EirGrid TSO and those conditions which operate on the basis that SONI will be an independent TSO).

2.58 The new Condition 42 to be introduced to the SONI Transmission Licence addresses these four areas of concern by means of new licence obligations which make provision in relation to each of the following:

- The composition and functions of the SONI board of directors, in order to require SONI to establish an appropriately-empowered board acting with a sufficient degree of independence;
- The starting point of requiring SONI to ensure the managerial and operational separation of the SONI TSO business from EirGrid and any other company within the EirGrid Group;
- The potential for SONI TSO to be exempt from this separation requirement in respect of those business functions for which it has been granted a derogation by UR and to such extent (and subject to

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<sup>47</sup> In the Call for Evidence we effectively ruled out the option of maintaining the status quo (see Paragraphs 7.3-7.5 of the Call for Evidence). At that stage we considered that, as a minimum, Condition 12 of SONI's licence needs amendment to achieve greater clarity and we identified three further options for change for the governance arrangements. The options set out in the Call for evidence were not proposals for action; they were included as a vehicle for discussion of the issues, by way of indicating the kinds of policies that could be developed by UR if Call for Evidence identified any issues that need to be addressed.

The remedies to address the issues observed with regard to the governance of SONI TSO were set out in section 6 of the April Consultation Paper and these took the form of four distinct options for change, each of which envisaged different degree of change to the independence of the SONI board and the independence of SONI management. All the options included a number of other governance changes to strengthen protections for NI consumers. The options were explained in detail in section 6 of the April Consultation Paper and there is also a summary table providing an overview (see from page 52 of the April Consultation Paper). In April 2021 our provisional preferred options were Options B and C (see Paragraphs 6.67-6.69 of the April consultation paper) and these were later narrowed down to option C in the Consultation on licence modifications published in January 2022.

such conditions) as UR may determine – the board of SONI having first applied for that derogation and demonstrated to UR that it is appropriate and will operate in the interests of NI consumers; and

- The requirement for SONI to develop a compliance plan and appoint a compliance officer in relation to the new licence requirements.

- 2.59 At the Board level, the new licence requirements are designed to reflect good practice in corporate governance, and will ensure that the SONI Board has the balance of skills, knowledge and experience appropriate for the TSO business, and that Board level decision-making in SONI is appropriate in scope and is independent of EirGrid plc. This will enable the SONI Board to fulfil the role of the ‘guiding mind’ of the TSO business in a manner which is transparent and accountable to UR and other stakeholders and provides assurance that the interests of NI consumers are being protected by SONI.
- 2.60 Similarly, the requirement for managerial and operational separation of the SONI TSO business from EirGrid will provide for greater transparency and accountability in relation to decision-making by the SONI TSO business. Managerial and operational independence from EirGrid in the performance by SONI of its TSO activities and functions will lead to dedicated resource for the TSO business (wherever required) and ensure that it is appropriately focused on its core task of acting as TSO in respect of NI and with a view to protecting the interests of NI consumers.
- 2.61 However, UR wants to ensure that the licence condition will operate in a flexible and proportionate manner, and has therefore made provision under the new condition to grant derogations from the separation requirement to the extent that the integration of managerial or operational functions can be justified as best serving the interests of consumers. This presents a question for the newly-independent SONI Board. The licence condition offers the Board the opportunity to identify those functions, systems and processes that (in its view) require to be integrated with those of EirGrid plc in order to support the SEM, or which the Board considers should remain integrated for other reasons that are consistent with protecting the interests of NI consumers.
- 2.62 The first effect of the licence condition therefore will be to require the SONI Board to address its mind to these issues, and to consider when integration can and cannot be justified – a process that there is no evidence has taken place historically. If there are business functions in respect of which the Board believes that integration can be justified, it will have the opportunity to make its case to UR for maintaining the existing integrated functions in those areas, or adopting a different form of integrated approach. This case for a ‘derogation’ from the separation requirement would need to evidence the

tangible efficiencies for NI consumers delivered by integration and/or demonstrate that SONI would be materially more effective in carrying out its operations than would otherwise be the case – in all cases while still maintaining an appropriate level of independent SONI decision making and accountability.

- 2.63 Consequently, the derogation process will provide an opportunity to assess the evidence for the need for joint working with EirGrid, and will also improve transparency over SONI's costs and how those are shared with EirGrid. UR or SEMC (as the case may be) will be able to scrutinise SONI's proposals for continued functional integration with EirGrid plc and ensure these are in the interests of consumers. The power within the new licence condition to award any derogations on a function-by-function basis, and to grant them subject to conditions which may limit them in scope or provide for the derogated-activity to be regulated in a particular way, is designed to ensure that this jurisdiction can be exercised flexibly to meet the circumstances of individual cases.
- 2.64 The placing of a time limit on derogations means that they will be reviewed every few years to ensure that they are working as intended and continue to be in the interests of consumers. On the other hand, the refusal to grant a derogation on the first request does not mean that the business function to which it relates can never be operated on an integrated basis; after a gap of a suitable period, it will be open to SONI to try to make the case again for a derogation, providing new and better evidence if it is able to do so.
- 2.65 Taken overall, the derogation process is an important mechanism to ensure that the SONI Board and management actively consider how SONI TSO licence obligations are best delivered to the benefit of consumers. The SONI Board will be responsible for the derogation applications and the evidence to support them, and the onus will be on it to justify why they should be granted. This process will radically improve the transparency (in particular the visibility for UR and SEMC) of the relationship between SONI and EirGrid, while making the SONI board accountable for demonstrating why any preferred degree of integration with EirGrid is the best means to fulfil its obligations as a TSO. It also ensures that the new licence condition will be able to operate proportionately and flexibly, by providing that the separation obligation need not be enforced to the extent that it is in consumers' interests not to do so.
- 2.66 Overall the increased independence at Board and management level in SONI, coupled with appropriate governance mechanisms (e.g. a condition of a derogation requiring the existence of an SLA) where services continue to be delivered through the integrated Group structures, will ensure effective oversight by UR of decisions made by SONI in regard to how its licence obligations are delivered. The new licence condition will open up the 'black



box' we see at present, ensuring that the TSO activities are transparent, open to regulatory scrutiny, and therefore fully accountable to the interests of consumers in NI who ultimately fund the TSO. This will allow any problems to be revealed over time and enable the regulator, where necessary, to take corrective action. In this way the licence modifications will enable UR and SEMC to regulate more effectively.

- 2.67 Greater TSO independence and the derogation process itself will support SONI in focusing on and articulating the interests of NI consumers, ensuring a greater alignment between the shareholder and NI consumer objectives. In turn this will drive increased confidence among the wider group of stakeholders in the development, operation and management of the NI transmission network, including in particular in respect of the transition to a low carbon economy.
- 2.68 The new licence condition will lead to greater independence of decision-making and separate resources where needed to meet licence obligations to act in conjunction with EirGrid or otherwise bolster the capability of SONI. The licence changes will restore an appropriate level of independence to SONI, which will allow it to act in conjunction with EirGrid TSO and participate in SOA structures in the manner that was always intended under the licence. This will facilitate the SEM regulatory framework to work as it was originally designed to do.
- 2.69 In addition, SONI TSO will also be able to better document compliance with other licence conditions of its licence, e.g. on availability of resources and prohibition of cross subsidies.

## **UR statutory duties**

- 2.70 This section sets out examples illustrating how the new licence condition furthers UR's principal objective and general duties under Article 12 of the Energy (Northern Ireland) Order 2003.
- 2.71 The UR's principal objective in relation to electricity matters, including the licensing regime under which SONI TSO operates, is:

*"To protect the interests of electricity consumers in Northern Ireland, wherever appropriate by promoting effective competition between persons engaged in or in commercial activities connected with the generation, transmission or supply of electricity."*<sup>48</sup>

- 2.72 The modification facilitates the UR's principal objective as it secures the interests of both present and future NI consumers through improved

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<sup>48</sup> Article 12(1) of the Energy Order.

governance which better aligns the commercial interests of SONI's shareholder with the interests of NI consumers. The modification will also increase transparency and accountability in SONI TSO. Increased transparency as to how SONI discharges its TSO licence obligations will ensure that the TSO's activities are properly open to regulatory scrutiny, problems can be revealed over time and the regulator can take corrective action to protect the interests of NI consumers where needed. As explained above and in the Preceding Documents, the governance review has revealed issues with transparency, e.g. in regard to TSO decision-making and cost information, which the measures in the licence condition will correct through increased Board and management independence in SONI.

2.73 Our duty is to protect the interests of NI consumers “wherever appropriate by promoting effective competition”. In the course of the governance review, less evidence of potential harm to competition emerged compared to the evidence of other potential harms.<sup>49</sup> However, the evidence was such that we were concerned that there could be potential barriers to competition whereby the shared management and operating model employed across EirGrid and SONI TSOs risks a one size fits all approach and potentially denies differences in developing and operating the NI network, including in system analysis and planning.<sup>50</sup> We consider that the licence modification will therefore promote effective competition by requiring that decisions are made by an independent SONI Board which is equipped with a broad balance of skills, knowledge and expertise so as to make expert decisions which appropriately balance the needs of multiple stakeholders and reflect the particular perspective of NI policy, issues in NI and the NI consumer.

2.74 In carrying out its functions, UR should also act in the manner best calculated to further the principal objective, having regard to:<sup>51</sup>

- The need to secure that all reasonable demands in NI or Republic of Ireland for electricity are met; and
- The need to secure that licence holders are able to finance the activities which are the subject of obligations imposed under NI energy law.

2.75 SONI has responsibility for planning the NI transmission network and does so in consultation with EirGrid TSO and with NIE Networks as transmission and distribution system operator. SONI TSO's responsibilities in this area are governed by licence conditions, such as Condition 40 (Transmission

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<sup>49</sup> See April 2021 Consultation Paragraph 4.14 and the January 2022 Consultation Paragraph 2.15.

<sup>50</sup> See April 2021 Consultation Paragraph 5.13 and January 2022 Consultation Paragraph 1.9

<sup>51</sup> These matters are set out at Article 12(2) of the Energy Order.



Development Plan NI).

- 2.76 The modification will further the principal objective by ensuring that SONI TSO is accountable to UR and NI stakeholders when planning the NI network. It will also ensure that, when discharging its all-island TSO duties jointly with EirGrid TSO, SONI can articulate and bring a NI jurisdictional perspective to joint TSO decision making, thereby enabling both TSOs to reach conclusions which ensure that the overall outcomes from the SEM are a win-win for both sets of consumers. The licence modification supports SONI in asserting an NI voice in joint TSO decision-making and so ensures that the reasonable demands in NI or Republic of Ireland for electricity will be met.
- 2.77 The modification is expected to give rise to increased costs associated with the ongoing maintenance of an independence SONI board and good governance mechanisms more generally. These were set out in the cost benefit analysis (CBA) contained in the April 2021 consultation paper, and UR is satisfied that that are necessary costs to ensure good governance and can be allowed (and regulated as to their efficiency) using existing price control mechanisms. They pose no issues in regard to financing SONI's activities.
- 2.78 The UR recognises that future costs will be incurred by SONI if the management and operation of certain business functions needs to be separated from the rest of the EirGrid Group. However, we do not know at this stage what derogations will apply so these costs cannot be assessed at present. SONI's points on the cost impact of the UR's proposals and the UR's view on these are set out from 3.62-3.87 below. However, we do not have any concerns that the amendments will lead to SONI being unable to finance the activities which are the subject of obligations imposed under NI energy law. We also note that our duty in relation to financeability will apply in any subsequent related decisions; for example, we will consider it when assessing any application for a derogation and in subsequent price control decisions, and it will remain open at that point for SONI to draw attention to likely costs and for UR or SEMC to consider these when determining if and to what extent to grant a requested derogation.
- 2.79 UR is also required to carry out its respective electricity functions in the manner which it considers is best calculated:<sup>52</sup>
- To promote the efficient use of electricity and efficiency and economy on the part of persons authorised by licences or exemptions to supply, distribute or participate in the transmission of electricity;

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<sup>52</sup> These matters are set out at Article 12(5) of the Energy Order.

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

2.80 We consider that the decision to introduce Condition 42 will introduce a more independent, transparent and accountable SONI TSO, which reflects the interests of NI consumers and ensures a win-win for consumers in both NI and Republic of Ireland. This will further the objectives set out above. The matters listed in Article 12(5) also fall to be considered by SONI in the context of the energy transition. NI government policy requires a move to low-carbon forms of generation in the generation mix and this transition will progressively increase the challenges of operating the electricity system in a stable, sustainable, safe and secure manner, at least cost. The energy transition may also result in some policy divergence between Republic of Ireland and NI over time. For example, it is possible that the types of generation connected to the systems of NI and Republic of Ireland will differ. These differences in turn then deliver different benefits and challenges in operating and developing the associated power system and networks. See Annex 5 which sets out a number of examples of areas where policy divergence between NI and Republic of Ireland may occur and, if not managed appropriately by SONI TSO, could act to cause harm to consumers.

2.81 As SONI is a key delivery body for the energy transition, a key aim of the governance review is to ensure that SONI TSO's governance arrangements are fit for purpose into the future energy transition. The modification will ensure SONI is an effective and well-led TSO which is responsive and accountable to the needs of stakeholders for how it manages the challenges of the energy transition. It will also underpin the independence of SONI TSO and therefore promote trust in SONI's advice for UR and NI government on

dealing with the challenges ahead in the best interests of NI consumers.<sup>53</sup>

### **3. Stakeholder feedback on the statutory licence modification consultation**

- 3.1 Responses were received from EirGrid and SONI and the following paragraphs summarise those responses.
- 3.2 Neither EirGrid nor SONI supported the licence modifications to change SONI's governance proposed by UR. The individual EirGrid and SONI responses made a number of specific points, some of which have common themes.

#### **Key points from the EirGrid response**

- 3.3 In EirGrid's case, the key such comments are summarised in the following paragraphs, grouped into the following subject areas<sup>54</sup>:
- Impact of SONI governance changes on the EirGrid Group;
  - UR's approach is neither balanced nor well-reasoned;
  - The licence modifications are a SEM matter;
  - UR's misportrayal of EirGrid's response;
  - Response to the proposed licence modifications; and
  - UR's proposed derogations process.
- 3.4 The EirGrid response also included an annex setting out what it claims to be allegations and false premises included in UR's April consultation paper.

#### ***Impact of SONI governance changes on the EirGrid Group***

- 3.5 EirGrid is concerned about the impact of SONI governance changes on the EirGrid Group. In particular, it is concerned that the new independent SONI Board will affect the decision-making process across the entire EirGrid Group, and will affect the ability of the EirGrid Board to exercise oversight over SONI Ltd and so will force an organisational restructure to ensure

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<sup>53</sup> A number of the responses to the Call for Evidence discussed the importance of trust, transparency and accountability in SONI TSO (e.g. CCNI, Paul Frew MLA). Also section 2 and annex 3 of the April consultation paper discussed a number of examples where regulators and regulated companies have driven or proposed changes in governance to aid trust and stakeholder influence.

<sup>54</sup> These follow the structure of the EirGrid response.

compliance with SONI TSO's licence.

- 3.6 EirGrid also notes that the proposals run counter to the legislative requirements in Republic of Ireland (no NI equivalent is cited) with respect to the Code of Practice for the Governance of State Bodies to which both EirGrid and SONI, as a subsidiary, are subject, and which are specifically designed to promote good governance. EirGrid notes that it will be seeking indemnification in respect of any liabilities or losses arising out of UR's proposals.

### ***UR response***

- 3.7 The licence modification will alter the balance of responsibility between the EirGrid plc Board and the SONI board, but in respect of SONI TSO matters only. It will also alter the composition of the Board of SONI Ltd, as this is the legal entity that holds the SONI TSO licence.
- 3.8 EirGrid does not specify specific examples for how the introduction of an independent SONI Board will have an adverse effect on the decision-making process across the entire EirGrid Group. The licence modification will alter the balance of decision-making between SONI board and management and the EirGrid plc Board and EirGrid Group executives. Changes to the EirGrid plc board scheme of delegation may be needed in consequence. However, the EirGrid Group integrated management structure would continue to apply to Group companies located in Republic of Ireland. Where SONI proposes that licence obligations are to be delivered through EirGrid integrated structures, then the derogation application will need to set out the arrangements with EirGrid plc for use of shared managements and resources. However, it is not possible to pre-empt what these might be now.
- 3.9 We also note that in regard to oversight by EirGrid of SONI that the licence modification allows EirGrid to appoint one member of the SONI Board. Also, that the parent company's role under the Companies Act 2006 is not affected by the licence modification as paragraph 15 of Condition 42 makes clear.
- 3.10 However, in any event, EirGrid is the parent company of a highly regulated licensed business in NI, which it chose to acquire in full knowledge of the nature and scope of the regulatory regime. It is aware that its subsidiary must comply with all relevant NI law and regulation from time to time. And it therefore should expect that the regulator may wish to make governance adjustments from time to time, including changes to the composition of the SONI board, particularly where the changes have been identified as appropriate in order to promote the interests of NI consumers. Other utility regulators have made licence changes requiring similar changes to governance to those proposed here. A number of such examples were set out in Annex 2 to our April 2021 consultation paper, most notably relating to

the GB Electricity System Operator and English and Welsh water companies. The position on the GB Electricity System Operator has developed further since the publication of the consultation paper, with the UK Government now additionally introducing legislation into the Westminster Parliament to the effect:

- That the System Operator should have licence duties relating to energy consumers;
- That the System Operator should abide by relevant strategy statements issued by Government; and
- That the System Operator should move to being state owned.

3.11 EirGrid does not specify how UR's licence modification would cause SONI or EirGrid to breach the Code of Practice for the Governance of State Bodies in Republic of Ireland but in any case the primary legal and regulatory framework which applies to SONI is the UK/NI framework. We note the suggestion that the licence condition would trigger changes to SONI's Articles of Association and that this requires Ministerial consent in Republic of Ireland. We expect that EirGrid as shareholder will do everything necessary to ensure that its subsidiary SONI can comply with all its legal obligations. See section 4 which explains changes to licence modifications consulted on in regard to the Articles of Association.

***UR's approach is neither balanced nor well-reasoned***

3.12 EirGrid states that: it has always acted reasonably and rationally in seeking to 'maximise benefits for consumers on the island';<sup>55</sup> and EirGrid and SONI have become further integrated over the past few years by virtue of regulatory decisions such as the I-SEM. It says the integrated structures allow for economies of scale which ultimately benefit consumers in Republic of Ireland and NI. EirGrid states that while the current licence provides that such synergies can be realised, the new modification proposed by the UR does not.

3.13 EirGrid then maintains that UR has failed to properly consider the impact the proposals will have on future costs to consumers or the risk of future harm to consumers arising from the impact on the SEM. It is not clear why the modifications are necessary to mitigate the risk of future harm when no evidence of harm has been evidenced. EirGrid does not believe that the modifications will benefit NI consumers.

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<sup>55</sup> EirGrid response, Paragraph 13.

- 3.14 EirGrid also alleges a failure on UR's part to meaningfully engage with EirGrid on SONI governance and alleges that there is some 'wider unexplained motivation' shaping UR's approach to SONI TSO governance.<sup>56</sup>

***UR response***

- 3.15 It is not UR's intention to create barriers to smooth and joint working between the TSOs provided there is sufficient transparency and accountability within their joint working arrangements to enable UR to assure itself that NI interests are considered and NI consumers are treated equitably and fairly. Accordingly, the derogation process is designed to allow the benefits from economies of scale and synergies to be revealed by SONI so that they can continue to be captured for consumers in a manner which is transparent and accountable.
- 3.16 As regards future costs to consumers, the derogation process will flush out the costs and benefits of SONI's current level of integration with EirGrid, presuming SONI applies for derogations in areas where it is presently integrated with EirGrid. We cannot pre-empt the outcome of the derogation process and therefore the only costs that can be estimated at this stage with any accuracy are the costs of implementing the new independent board. We acknowledge that these Board costs will vary depending on the number of sufficiently-independent directors which SONI ultimately appoints.
- 3.17 In regard to the absence of evidence of harm, SONI made similar points in its response to the April 2021 consultation paper. These were addressed by UR in section 4 of the January 2022 licence modification consultation. Put simply UR does not always need to identify concrete harm before it can act. A real risk of harm is sufficient. The benefits of UR's proposals were set out in the CBA published in the April consultation paper and updated in the January 2022 licence modification consultation. That said, UR does consider that there are real life instances of a lack of transparency and of the interests of NI consumers being lost or overlooked under the current governance structure: see Annex 7.
- 3.18 UR rejects the allegation that it has failed to engage meaningfully with EirGrid on SONI governance. The January 2022 licence modification consultation was the third in a series of consultations on this topic and it has carefully considered each response EirGrid has submitted. UR has facilitated meetings with EirGrid, including to discuss governance issues. In short, the process has been full and extensive, and UR is satisfied that EirGrid has had an appropriate opportunity to make all of the points that it would wish to make. It is not clear what concrete steps are said to be lacking and which

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<sup>56</sup> EirGrid response, Paragraph 22.

EirGrid would regard as ‘meaningful engagement.’

- 3.19 We also reject the view that there is an unexplained motivation shaping the UR’s views on governance. The new licence condition furthers the UR’s statutory duties as explained in section 2.

***The licence modifications are a SEM matter***

- 3.20 EirGrid’s view is that ‘as a matter of logic’ the licence modifications are a matter for SEMC not UR. It places emphasis on the fact that the Memorandum of Understanding (MOU) between the two Governments which underpins the SEM, states that the SEM arrangements will be designed to promote a ‘single competitive, sustainable and reliable market in wholesale electricity in Northern Ireland and Ireland,” and that All-Island Energy Market Development Framework provided for consideration of a single electricity TSO on the island of Ireland, a consideration which EirGrid states subsequently underpinned the SEM Order. EirGrid believes that the governance changes are counter to the intent of the two Governments and it notes the range of activities carried out on an all-island basis by the TSOs acting on conjunction.

- 3.21 In summary EirGrid notes that-

*‘The decisions made today jointly on an all-island basis in the interests of consumers will, if made separately and with a purely jurisdictional focus, influence the outcome of the SEM and ultimately impact the cost to market participants.’<sup>57</sup>*

***UR response***

- 3.22 The SEMC has considered whether it wishes to call in the licence modifications as a SEM matter and has decided not to do so.<sup>58</sup>
- 3.23 Furthermore, we note that the licence modification is consistent with SEMC policy at the time of SONI acquisition by SONI. It is designed to ensure that SONI TSO has sufficient independence from EirGrid to allow it to act in conjunction with EirGrid TSO as the regulatory scheme for the SEM intended. See annex 6 for a fuller explanation.<sup>59</sup>
- 3.24 EirGrid implies that the creation of a single electricity TSO is underpinned by the SEM Order and its equivalent in Republic of Ireland, but this is not the

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<sup>57</sup> Paragraph 30 of the EirGrid response.

<sup>58</sup> UR has kept the SEMC informed as the review has progressed as the Proceeding Documents illustrate. See page 8 of the April Consultation Paper and Paragraph 3.56 of the January 2022 Licence Consultation paper.

<sup>59</sup> In the Proceeding Documents also, see Paragraphs 3.17-3.25 of the January 2022 Licence Consultation Paper which explained how the regulatory framework for the SEM should operate.



case: see Annex 6. The original proposal of the two governments for the all-island energy market did include the establishment of a single electricity system operator for NI and Republic of Ireland, but in the end this proposal was not adopted and so was not included in the SEM Order. The Order only dealt with establishment of the market arrangements for the SEM.<sup>60</sup> It is not for EirGrid unilaterally and without appropriate legislative or regulatory basis or blessing to design and implement its own proposed system outside the approved legislative regulatory framework.

### ***UR's misportrayal of EirGrid's response***

- 3.25 EirGrid does not agree with UR's view that "*there is no independent SONI view*" and that "*There is no SONI 'guiding mind' on the Board such that UR's vision of good governance could be fulfilled.*"
- 3.26 Nor does EirGrid agree with UR's view that for the impacts as set out by EirGrid and SONI to eventuate, SONI (and/or EirGrid) will need to act irrationally. EirGrid considers that UR has failed to consider scenarios where two independent economically rational agents acting in their own interest do not reach the same outcome as two economically rational agents acting together in a common interest. EirGrid takes the view that under UR's proposals both EirGrid and SONI would be required to operate with an economic rationale which sought to maximise their own interests even if at the expense of the other, and that this contrasts with the situation which currently pertains where both act in the common interest.

### ***UR response***

- 3.27 We note that EirGrid does not agree with some of the views expressed by UR but that is not the same thing as a factual inaccuracy or a mischaracterisation, still less an error of assessment by UR on a topic on which views can reasonably differ. UR's conclusions on governance are based on information provided by EirGrid and SONI about the level of integration between the two, and which EirGrid itself describes as a 'heavily integrated structure.'<sup>61</sup> These were set out in the April 2021 consultation paper which included a description and assessment of SONI's current governance arrangements.<sup>62</sup>
- 3.28 Furthermore, we reject EirGrid's view that as a result of governance changes, it and SONI would be required to operate with an economic rationale which sought to maximise their own interests even if at the expense of the other. This view is contrived, not least since it completely ignores the

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<sup>60</sup> See Paragraphs 10 and 11 of the Explanatory Memorandum to Electricity (Single Wholesale Market) (Northern Ireland) Order 2007.

<sup>61</sup> Paragraph 14 of the EirGrid response.

<sup>62</sup> Section 3 and Annex 2 of the April 2021 Consultation Paper.

fact that, for SEM purposes, both TSOs are required to act in conjunction, to cooperate, and to collaborate with each other by virtue of licence conditions which are not altered in any way by UR's governance changes. More fundamentally, EirGrid's view ignores the fact that the 'common interest' of Irish and NI consumers can only be safeguarded by two independent TSOs operating within regulated structures that enable collaboration and cooperation in a transparent and accountable way.<sup>63</sup> The present 'heavily integrated structure' is designed to deliver outcomes efficiently but in a unitary fashion which obscures a jurisdictional perspective, and so risks underplaying or suppressing the potentially divergent interests of NI consumers in particular. The lack of independence of the current SONI board, the 'internalisation' of the SOA, and the lack of a SLA between the TSOs are all conspicuous outworkings of this in the governance structure. UR's licence modification is the minimum needed to correct this situation.<sup>64</sup>

### ***EirGrid response to the proposed licence modifications***

3.29 The following are the broad themes in EirGrid's response on the text of Condition 42. See Annex 4 for a more detailed summary.

- Inconsistency with existing EirGrid plc licence conditions, in particular the requirement to act in conjunction with SONI TSO;
- Inconsistency in treatment compared to other licence holders, notably NIE Networks, and no basis for UR role in the appointment of directors which EirGrid considers amounts to an approval role for UR;
- Impingement on EirGrid's rights as owner and shareholder – notably that EirGrid plc may appoint only one member to the SONI board – and that UR's proposals for SONI go much further than what is in

<sup>63</sup> We have previously explained how collaboration between the TSOs is fundamental to the SEM and how the regulatory framework is designed to enable it. See Paragraphs 3.17-3.28 of the January 2022 consultation paper.

<sup>64</sup> The April 2021 Consultation Paper included four options (A, B, C, and D) to change SONI's governance. The licence modification is prepared on the basis of Option C. Option A was ruled out because it does not go far enough to meet our vision for SONI governance and provide sufficient protection for NI consumers. Option D, while a viable option to address the risks identified in SONI's current governance, was ruled out because it could potentially remove all of the efficiencies that could be gained between the TSOs. However, we noted that in the context of the SEM arrangements, an operating model based on Option D is tenable and indeed the SOA envisages collaboration between two separate TSOs. The January 2022 licence modification consultation assessed option B compared to C. The key difference between them is that Option C puts the evidential burden on SONI to make a robust case for a 'derogation' from the requirement for independence. Option C was preferred compared to B on the basis that Option C will lead to more evidence based outcomes that are the product of a considered derogation request by an independent SONI Board. The derogation process in option C and any subsequent applications for derogation will be important in beginning to build a culture of transparency and accountability in SONI. Accountability and transparency will therefore be stronger under Option C than B. We also note that of those respondents to the April 2021 consultation who expressed a preference for any of the options consulted on by UR, more respondents favoured Options C and D than favoured Options A and B.

place for NIE Networks;

- The modification would contravene the current legal framework in place for EirGrid and is therefore unworkable;
- UR portrays a prejudice against EirGrid when compared to NIE Networks and Mutual Energy Ltd (MEL);
- EirGrid has not been afforded any substantive engagement with UR as part of the governance review.

### *UR response*

3.30 The following is a summary of UR's response to the broad themes in EirGrid's response on Condition 42. See Annex 4 for a more complete UR response to the issues raised.

- The SEM requires acting in conjunction, collaboration and cooperation between the two TSOs but not integration of TSOs or the creation of a single TSO. See Annex 6 of the decision paper which explains more fully how this concept should work.
- UR's approach to SONI board appointments is not inconsistent with its role in NIE Networks board appointments as UR has a similar role in NIE Board appointment to that proposed for SONI. See Condition 3A (1)(b) of the NIE Networks Participate in Transmission licence. We acknowledge that ESB retains ultimate responsibility for appointments to the NIE Networks board whereas this will not be the case for EirGrid and appointments to the SONI Board. However, NIE Networks' relationship with ESB is currently characterised by separation not integration and ESB and NIE Networks have no need to act in conjunction for SEM purposes. Therefore more stringent governance structures can apply to SONI compared to NIE Networks.
- Impingement on Eirgrid rights as shareholder is necessary in order to ensure an independent SONI TSO.
- We do not agree that the licence condition contravenes the current legal framework in place for EirGrid and is therefore unworkable. The proposals can legally be implemented in accordance with Irish law once the consent of the Minister is obtained. In regard to the Republic of Ireland Code of Practice for the Governance of State Bodies we note that SONI is subject to the UK legal framework including the licence under which SONI operates. But, the UK framework is not

subject to the Republic of Ireland Code of Practice. It is for EirGrid to reconcile the requirements of the code with UK rules applicable to SONI.

- We disagree with EirGrid's views on bias with reference to the MEL governance review. MEL is a mutual company, unique in the NI energy industry and therefore very different to the EirGrid Group. MEL's response to the January licence modification consultation noted that MEL's governance arrangements are not analogous to that of SONI within the EirGrid Group. We agree – therefore the outcomes of the two reviews cannot be compared.
- We also reject the allegation that we have failed to engage meaningfully with EirGrid on SONI governance. See paragraph 3.18 above.

#### *UR's proposed derogations process*

3.31 The following are the broad themes in EirGrid's response to the derogation process. See Annex 4 for a more detailed summary.

- Will give rise to significantly greater costs to the SONI business and NI consumers as an SLA will result in the attribution of services on the basis of commercial terms rather than cost attribution;
- Despite the derogation process there is no situation where the current arrangements could be expected to continue;
- Likely wide extent of derogations that will be needed in order to deliver the activities encompassed by the SOA and the licence obligations to coordinate, co-operate and act in conjunction;
- The derogation process creates four hurdles to achieve economic synergies where there are none at present;
- Potential for EirGrid to breach its TSO Licence solely on the basis of action, or inaction by SONI or by an absence of the UR taking the appropriate decisions;
- Require corollary amendments to the EirGrid licence, in particular Condition 3 in regard to the exercise of EirGrid functions in the interests of consumers in both Republic of Ireland and NI; and
- In order to be consistent with the existing framework UR would need to exclude the new condition from applying to 15 of SONI's TSO licence conditions at which point EirGrid considers the new condition would effectively become meaningless.

### *UR response*

3.32 The following is a summary of UR's response to EirGrid's points on the derogation process. See Annex 4 for a more complete UR response to the issues raised.

- An SLA would be a fundamentally different and transparent approach compared to the current Cost Allocation and Recharge policy. However, we do not agree with EirGrid's view is that an SLA is likely to give rise to significantly greater costs than the current arrangements as it would be based on an 'arm's length' arrangement on the basis of commercial terms rather than costs attribution. An SLA would not result in EirGrid and SONI having any commercial incentive to treat each other as unrelated companies each seeking commercial advantage, as this would likely result in increased costs for all consumers for common services, the underlying costs of which would not change. UR would not agree to inefficient costs (including a margin) in circumstances where costs could otherwise be allocated fairly by means of an agreed cost attribution approach governed by an SLA.
- Any current arrangement which is the subject of a successful application for a derogation from the independence requirements may continue. The scope and number of derogations to apply for is a matter for the SONI Board and there is no limit on the number that may be applied for.
- The derogation process is designed to ensure transparency and evidence based outcomes, the issues identified by EirGrid fall to be managed by SONI.
- The Condition 42 derogation process contains clear timescales for SONI and UR. Also where an application for derogation has not been granted by UR by the necessary date it shall be deemed granted in accordance with the provisions of Condition 42 Paragraph 28.
- For the reasons set out in the January 2022 consultation our governance proposals do not disturb EirGrid licence Condition 3 (see from 5.4-5.6 of the January 2022 paper).
- The 15 licence conditions cited regulate EirGrid/SONI interactions or otherwise require SONI to act in conjunction with, in co-operation with, or in consultation with EirGrid TSO. The derogation process itself will determine whether certain Business Functions should be exempt from the general requirement to be managerially and operationally independent from EirGrid. These decisions cannot be pre-determined

now in the absence of evidence to support them.

### ***EirGrid Annex 1***

- 3.33 Annex 1 of the EirGrid response lists a number of statements in UR's April 2021 consultation paper which EirGrid regards as allegations, false premises, or factual inaccuracies which could mislead the reader.

### ***UR response***

- 3.34 We have assessed all the points made in annex 1 and the majority echo points made elsewhere by EirGrid. No factual inaccuracies have been identified. The reasons for UR's view on these points were explained in the April 2021 consultation paper. EirGrid does not agree with UR's assessment. But this does not mean UR has made an allegation, false premise or a factual inaccuracy which could misdirect the reader.
- 3.35 Citing the definition of 'separate resources' in Condition 42, EirGrid questions our view that the licence modification will not affect SONI's SEMO and NEMO activities being carried out from the same premises as the TSO business. SONI Ltd is licensed as both SONI TSO and SEMO in NI. SONI staff working on SEMO issues can carry out their roles from the same premises. However EirGrid staff working in SEMO roles are part of an Associated Company, therefore SONI TSO will need a derogation that permits SONI TSO staff and EirGrid SEMO/NEMO staff to carry out their roles from the same premises.

### **Key points from the SONI response**

- 3.36 Overall SONI considers that:
- The decision is wrong in law because:
    - ◆ The matters are SEM matters and should be decided by SEMC;
    - ◆ It cannot legally be implemented by reference to section 5 of the Electricity Regulation (Amendment) (EirGrid) Act 2008;
    - ◆ UR's vision is fundamentally at variance to SONI's obligations to secure generation adequacy and capacity across the island of Ireland including as required by virtue of Article 11A of the 1992 Order; and
    - ◆ The new Condition 42 is poorly designed and may not constitute

a lawful modification under either the 1992 or 2007 Orders;

- UR has failed properly to have regard to the carrying out of its principal objective under Article 12 of the 2003 Order;
- The Modifications fail to achieve, in whole or in part, the effect stated by the UR;
- The Decision is based wholly or in part on errors of fact; and
- Procedural impropriety in UR's consultation process.

#### *UR response*

3.37 We do not agree that the decision is wrong in law:

- a) See from 3.50-3.54 below for our response to SONI's position that the matters are SEM matters. Similar concerns were raised by EirGrid, see our response at 3.22-3.24 above. As noted the SEMC has considered whether it wishes to call in the licence modifications as a SEM matter and has decided not to do so.
- b) The proposals can legally be implemented in accordance with Irish law once the relevant Minister's consent is obtained. See our response to Paragraphs 52-57 of the EirGrid response set out in Annex 4.
- c) UR's vision is consistent with SONI's licence obligations in the all-island context which are themselves designed to further Article 11A of the Electricity Order 1992. See Annex 6.
- d) We do not agree that the new condition is poorly designed and note that no particular examples of poor design are set out in Paragraph 1.12 of SONI's response. See our response to SONI's points on the derogation process below. Also SONI's response on the drafting of the condition itself alleges, for example, that the drafting is insufficiently clear and precise, and that in some cases it contradicts other licence conditions. We do not agree with these points for the reasons set out in Annex 3.

3.38 SONI also considers that UR has failed to have regard to its principal objective under Article 12 of the Order. See section 2 (2.70-2.81) which illustrates how the new licence condition furthers UR's principal objective and general duties under Article 12 of the Energy (Northern Ireland) Order 2003.

3.39 We do not agree with SONI's view that the modifications fail, in whole or in part, to have their stated effect and our reasons are set out in Annex 3.



- 3.40 Similarly, we do not agree that any of the issues identified by SONI are errors of fact, see our response to the issues SONI raises with Option C at 3.55-3.58 below.
- 3.41 SONI also alleges procedural impropriety in regard to UR's consultation process and that UR has 'pre-determined the output of its consultation process from the outset'. Specifically SONI cites the length of the process, failure to identify evidence of harm, failure to elaborate on our proposals despite requests from SONI, failure to disclose a substantive CBA, failure to advance changes to Condition 12 or publish the guidance referenced in Condition 42. We do not agree with SONI's allegations of procedural impropriety and many of their specific points are addressed below or in our response to Annex 3. We also note that other respondents have noted the quality of UR's work to date on governance issues (see 3.93 below).
- 3.42 SONI also cites a failure by UR to elaborate on our proposals despite requests from SONI but this was not the case. The January licence modifications consultation was the third in a series of consultations on this topic and we have considered carefully each response SONI has submitted as well as seeking further information from SONI where necessary.
- 3.43 In SONI's case the key such comments are summarised in the following Paragraphs, grouped into the following areas:
- The licence modifications are a SEM matter;
  - Feasibility of the implementation of Option C;
  - Understated cost impact of the UR proposals; and
  - Response to the licence modifications.

***The licence modifications are a SEM matter<sup>65</sup>***

- 3.44 There are a number of strands to SONI's argument that the licence modifications are a SEM matter.<sup>66</sup>
- 3.45 Firstly, as SONI Ltd is a single legal entity, SONI argues that any consideration of its governance must be by reference to the corporate entity as a whole. Therefore UR's proposed approach of carving out what would be "the constituent part of SONI" within SEMO as being distinct from SONI in its capacity as TSO is irrational as a corporate construct.

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<sup>65</sup> See section 2 of the SONI response.

<sup>66</sup> Some of these arguments have been advanced in a judicial review against the UR and SEM-C. By Judgment dated 21 March 2022, Mr Justice Humphreys refused leave to apply for judicial review. That judgment is presently under appeal before the Court of Appeal in Northern Ireland.

- 3.46 Secondly, it argues that UR's proposals will materially affect the SEM and SONI cites the points it made in response to the April 2021 consultation, its assessment of the cost impact set out in section 4, and the case studies set out in the annexes as supporting evidence.
- 3.47 Thirdly, SONI considers that UR has misdirected itself as regards its statutory objectives in the context of a matter affecting the SEM. This is because, in the consultation, UR has referred to its principal objective of protecting the interests of consumers in NI under Article 12 of the 2003 Order. But this objective does not apply to functions to which Art. 9 of the SEM Order applies and where the principal objective of the UR in giving effect to any decision of the SEM Committee is to protect the interests of consumers of electricity in NI and Republic of Ireland.
- 3.48 Fourthly, SONI's core functions are matters that fall within the remit of the SEMC (e.g. Capacity Remuneration Mechanism (CRM) and Delivering a Secure, Sustainable Electricity System (DS3)), all areas which directly impact the SEM and the costs for which are provided by UR on the basis of no restriction on the integrated economic operation of the system across EirGrid and SONI or between licences. SONI also believes that UR proposals will cut across previous SEMC decisions and practice, therefore risking incoherent decisions which the 2007 order was created to avoid.
- 3.49 Fifthly, the SOA is designed to protect the interests of consumers in Republic of Ireland and NI but instead UR talks about each TSOs protecting the interests of their own consumers. Also SONI believes that the interests of one set of consumers have not been neglected and that UR's assertion that EirGrid views legitimate differences between Republic of Ireland and NI as small or non-existent is not representative of the facts. SONI also notes that it responded to UR's Art 51 notice received in August 2021 and notes that it has not received any feedback from UR since this submission.

### ***UR response***

- 3.50 In the January licence modification consultation paper, we responded to SONI's concerns about the impact of TSO governance changes on SONI Ltd as a corporate body. Also UR notes that the fact that the regulated entity is SONI Ltd has not prevented distinct roles being carved out from each other and regulated separately. The SONI SEMO and TSO roles are regulated under separate licences with separate price controls – the SEMO price control being decided by SEMC and the TSO price control by UR.
- 3.51 We do not agree that UR's proposals will materially affect the SEM. SONI made similar arguments in response to the April consultation paper. The further information presented in response to the January licence modification consultation (including the case studies) appears predicated on the view that

even with the derogation process full separation of functions will necessarily result from UR's proposals. There is no reason to presume that this will be the case and SONI has not clearly explained why, even in circumstances where a derogation is granted, there would be a material effect on the SEM.

- SONI's case study on the capacity market seems to presume that separation of the CRM auction system will result from the licence modification as SONI states - '*SONI has considered a number of options to establish whether SONI could remain compliant with its existing obligations in the CRM whilst also meeting the requirements of the proposed licence modifications, including where derogations are utilised. SONI has not been able to identify any viable options.*'<sup>67</sup> No reasoning is given for this view.
- SONI's case study on the impact of UR proposals on system operations states that '*under a model where local management accountability dominates, and where such local accountability is being taken with reference to a clear regulatory direction, in SONI that being the UR's stated Vision for SONI, it is only rational that each TSO acting as both power system and balancing market operator would require a separate set of IT systems over which it has full operational and capital investment control.*'<sup>68</sup> We do not agree with this perspective – on the contrary it would be rational for SONI to optimise good outcomes for NI consumers through a single set of IT systems where this maximises efficiency.

3.52 Derogations can be granted when a case to do so is made out by SONI and UR intends to exercise its discretion when dealing with derogation requests in a pragmatic and cost-sensitive manner. From the information already provided by SONI during the governance review, we consider that they may be likely to be able to make out a case for derogation in a number of areas, such as system operations.

3.53 UR has not misdirected itself as regards its statutory objectives. SEMC has not chosen to call the matter in, therefore UR's duties under the SEM Order do not apply. It is the case that some of the things SONI does are subject to decision by SEMC, such as future ancillary system services such as DS3. But this does not make SONI TSO governance axiomatically a SEM matter. In accordance with the 2007 SEM Order, SEMC may call in future derogation decisions and the fact that it can do so, where it decides that any such decision is a SEM matters, will ensure coherent decision-making. There is therefore no risk of incoherent decisions. See also Annex 6 which sets out

<sup>67</sup> SONI response annex 3, p.56-57.

<sup>68</sup> SONI response annex 4, p.59.

previous SEMC decisions, explains how SONI and EirGrid TSOs should interact for SEM purposes, and the key features of the regulatory framework for TSO interaction in the SEM. The new licence condition is designed to ensure that the SEM works as intended by bolstering SONI's independence vis-à-vis EirGrid in SEM structures.

- 3.54 Finally, for the reasons set out in the April consultation paper we do not believe that a meaningful SOA is currently in place with structures within which SONI can effectively act independently of EirGrid in articulating an NI perspective. See from 2.49-2.54 above for further details. We also note that ensuring SONI can act meaningfully in SOA structures is all the more important in circumstances where the two TSOs together are responsible for the content of the SOA and may modify the agreement without the approval of the CRU or UR.

### *Feasibility of the implementation of Option C*

- 3.55 Section 3 of the SONI response makes a number of points about the feasibility of Option C and the derogation process in particular. Many of these points are repeated in section 5 of the SONI response which addresses the licence modification drafting in more detail.
- 3.56 Firstly, SONI consider that UR has failed to fully assess the effect of the licence modifications and give notice of these, and therefore that the modifications proposed to the SONI TSO licence fail to achieve, in whole or in part, the effect stated by the UR and for this purpose points to Paragraph 6.2 of the January 2022 licence modification consultation as being where UR has stated the effect of the proposed modifications.
- 3.57 Secondly, SONI then lists a number of what it considers 'failures' in UR's assessment<sup>69</sup> which include –
- a) Alleged deficiencies in UR's cost benefit analysis;
  - b) Derogations are optional for SONI to request and UR retains full discretion as to whether a derogation should be granted. For the CBA to hold UR would have to presume that SONI will seek derogations and UR has predetermined they will be granted;
  - c) UR's proposal presents a legal inconsistency as if implemented it would render SONI in breach of Condition 23A from the effective date;
  - d) Use of derogations not being compatible or practical for SEM related obligations;

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<sup>69</sup> See Paragraph 3.4 (a) to (j) of the SONI response.

- e) The assumption that SONI will implement any additional conditions attached to a derogation;
- f) The assumption that EirGrid, SEMO and SEMOpx will agree to all requested and approved derogations;
- g) Unrealistic timeframes for the preparation of initial derogations;
- h) No consideration of implementation timeframes where a derogation is not granted or not sought;
- i) No consideration of implementation costs where a derogation is not granted or not sought; and
- j) No consideration of the additional costs on EirGrid, SEMO and SEMOpx as applicable, for the preparation and ongoing management of derogations and Service Level Agreements ('SLAs') and how these will be recovered.

3.58 Thirdly, while SONI acknowledges that UR's proposals 'appear to allow for some element of shared systems and resources on the basis of approval of a derogation',<sup>70</sup> SONI nonetheless believes that the derogation process has a number of limitations and would overall introduce a considerable administrative burden on SONI and will risk undermining the effectiveness of SONI functions in support of the SEM. Specifically SONI points to the fact that<sup>71</sup>:

- a) The derogation process fails to recognise SONI's obligations owed in the context of the all island operation of the SEM to consumers in both NI and Republic of Ireland;
- b) The derogation process fails to recognise that SONI is a single legal entity and SONI Board must seek to ensure that it fulfils its licenced functions with respect to the SEM / All Island Consumers as applicable;
- c) The derogation process directly impinges on the remit of the SEMC. SONI considers that it must seek and be granted a derogation in order to meet a number of licence conditions related to the SEM (e.g. Condition 22A scheduling and dispatch). See also the case studies in annexes 2-6 of the SONI response;
- d) The derogation process presents a dilemma due to the potential impact a derogation decision could have on other parties impacted by such

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<sup>70</sup> Paragraph 3.6 of the SONI response.

<sup>71</sup> SONI also considers many of these points to be errors of fact as they are also repeated in Paragraph 1.32.

decision (e.g. licensees/functions, Regulatory Authorities, Consumers and Market Participants);

- e) UR has failed to consider the impact of additional conditions imposed by UR when approving a derogation;
- f) The cost recovery for SONI and EirGrid activities associated with the operation of derogations and SLAs has not been set out;
- g) UR has failed to consider a realistic time period for the SONI Board to be established and then undertake a strategic assessment of what (if any) derogations should be progressed;
- h) Lack of guidance documentation on derogations process;
- i) Limitations of timeframes proposed by UR for implementation; and
- j) Impact on planned work such as SEM related initiatives including compliance to EU Network Codes as well as the delivery of the NI Energy Strategy.

### ***UR response***

3.59 In regard to SONI's first argument that UR has failed to fully assess the effect of the licence modifications and give notice of these, and therefore that the modifications proposed to the SONI TSO licence fail to achieve, in whole or in part, the effect stated by UR we note that:

- SONI points only to Paragraph 6.2 of UR's consultation paper as being a statement of the effect of the licence modification. In fact the reasons for and effects of the licence modification were set out in section seven of the January 2022 licence modification consultation. Accordingly, we disagree that the modifications proposed fail to achieve, in whole or in part, the effect stated by the UR.
- All the relevant statutory notice requirements were complied with – see the licence modification notice which was contained at annex 2 of the January paper.

3.60 In regard to SONI's second set of arguments – the items which SONI considers as 'failures' in UR's assessment<sup>72</sup> – we make the following points.

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<sup>72</sup> Items a) to j) listed at Paragraph 3.57 above.

- In relation to alleged failures a), b) and i) identified by SONI in respect of the CBA and the derogation process we note that in regard to the future cost impact of UR proposals:
  - ◆ The UR's CBA is based on the additional costs of implementing the new SONI board and new governance mechanisms (e.g. an SLA). These are simply the costs of good governance – greater independence, transparency, and capability in SONI to represent and deliver on the interests of NI government policy and consumers.
  - ◆ Additional costs may be incurred as a consequence of the derogation process, e.g. where a derogation is sought but not granted or alternative conditions are imposed. These future costs cannot and will not be known until the derogation process has been undertaken. It is therefore not possible to make an estimate at this stage. During the derogation process it will be for SONI to substantiate that integration with EirGrid brings benefits to NI consumers and that this is compatible with SONI's licence conditions such as Condition 24 and the 'acting in conjunction' obligations in the TSO licence. Moreover, since a refusal of a derogation will indicate that there are benefits to de-integration, then the costs of achieving that will need to be considered in the context of the benefits to consumers. This will be considered in the context of any derogation application.
  - ◆ If additional costs arise from the derogation process we expect these to be moderate (assuming no cross-subsidisation of EirGrid by SONI is revealed). When considering the need for derogations UR would expect that SONI as a reasonable and prudent operator (RPO) will make a case which optimises good outcomes for consumers and maximises efficiency. This may include either managerial independence or the seeking of a derogation. Derogations also have the potential to reduce costs by requiring SONI to use less expensive internal staff. Where no derogation is sought, it would be assumed that these conditions are already being met and no additional costs are required.
- Alleged failures c) and d) relate to whether derogations are practical for SEM related obligations. In this regard we note that SONI has already put forward information in section seven of its response to the April 2021 Consultation Paper to substantiate its view that the existing arrangements for single system operations have delivered benefits to consumers. Also, some of the information in the case studies annexed to SONI's response to the January licence modification consultation



begins to illustrate the benefits of integration, e.g. in regard to capacity market services in the SEM. This would need development into a robust cost benefit analysis but the information illustrates that SONI should be capable of providing a robust case with clear justification for a derogation in a number of areas.

- SONI describes as alleged failures UR's assumption that SONI can implement any additional conditions that UR may add to a derogation (failure e)) and the assumption (failure f)) that EirGrid, SEMO and SEMOpx will agree to any derogations approved. We do not regard these as 'failures' of our proposals, they are reasonable assumptions to take at this stage, particularly in the context in which SONI will be able to raise issues relating to implementation of proposed conditions in the course of the derogations process. In relation to point f) in particular, UR is entitled to assume that neither EirGrid nor SEMO will act in any way likely to cause SONI to breach its obligations under the licence as EirGrid plc has given an enforceable undertaking to this effect under Condition 3(11) of the SONI TSO licence.
  - ◆ Additionally, and related to point e), SONI's response expresses a wider concern that UR may attach conditions to a derogation. Consequently we have made an amendment to the licence conditions the effect of which is to encourage SONI to frame any potential conditions in its derogation application so that SONI's view on potential conditions may be considered by UR at the outset (see 4.27 below).
- Failure g) relates to SONI's view that the timeframes for the preparation of initial derogations are unrealistic. We consider that the timeframes are reasonable as SONI will have 15 months to prepare its derogation applications. Preparatory work to support the Board's decisions on derogation applications can commence before the new SONI board is appointed.
- Failure h) alleges that no consideration has been given to the timescales for implementation of alternative arrangements where a derogation is not sought or granted. The requisite timescales are set out in the licence modification (see Condition 42 Paragraph 20 and the meaning of the term 'Effective Date') and we consider that these are reasonable. Where a derogation is not granted SONI will have twelve months to effect separation and this balances the need to ensure SONI has sufficient implementation time with the need to ensure that separation occurs as swiftly as possible in circumstances where UR has decided a derogation is not in the interest of NI customers. Where

SONI does not apply for a derogation it will have at least one year to ensure separation.

- In regard to alleged failure j) see 3.86 below.

3.61 SONI's third set of points relate to what it sees as the limitations of the derogation process (see a) to j) at 3.58 above) we respond as follows.

- In regard to point a) and SONI's concern that the derogations process fails to recognise the all island operation of the SEM we acknowledge that a derogation decision could fall to be considered by UR under its statutory duties or by SEMC as a SEM matter and SONI will not know who will make the decision when making its application. Therefore we propose that guidance on matters that may be relevant for UR consideration and for SEMC consideration are set out in the Principles and Guidance document a draft of which will be published for consultation shortly (see also 4.28-4.29 below). SONI will be able to put forward its views on the design of the Principles and Guidance through that consultation process.
- Point b) is addressed at 3.50 above.
- As regards point c) we disagree that the derogation process necessarily impinges on the remit of SEMC, still less that the licence modification that puts in place the mechanisms for such derogation does so. The key point is that SEMC may call in any future decision on a derogation as a SEM matter, if it considers it necessary to do so. Where it does not do so, the remit rests with UR. Where a derogation is considered necessary by SONI to enable compliance with licence condition related to the SEM that is an issue which can be raised and considered in the course of the application for the derogation.
- In point d) SONI states that the derogation process presents a dilemma due to the potential impact a derogation decision could have on other parties impacted by such decision. The answer is that the derogation decision (and any associated decision about who bears any costs associated with separation) will be made in accordance with the relevant statutory duties of UR. In that sense there is no dilemma. If it transpires that a derogation made by UR reveals that arrangements put in place by EirGrid are not in the best interests of NI consumers, then who should bear the costs of any separation needed to restore regulatory conformity will be considered once the derogation decision has been made. We cannot rule out now the possibility that the shareholder may have to bear some of these costs.

- In regard to the potential impact of any conditions that may be attached to a derogation decision (point e)) – these impacts cannot be assessed in advance and in the abstract. We also note that for any derogation decision which SEMC decides is a SEM matter, then SEMC may also attach conditions to any decision it makes on a derogation application. See also 4.23 below which explains an amendment we have made to the licence conditions the effect of which is to encourage SONI to frame any potential conditions in its derogation application so UR can discuss and consider these in dialogue with SONI early in the derogation process.
- In regard to point f) cost recovery for SONI and EirGrid activities associated with the operation of derogations and SLAs – this was set out in the April 2021 consultation document. See 3.86 below where the assumptions used are repeated.
- In point g) SONI states that UR has failed to consider a realistic time period for the SONI Board to be established and then undertake a strategic assessment of what (if any) derogations should be progressed. We consider that the timescales for board appointment are reasonable to run this sort of recruitment exercise and planning for this need not wait until the licence condition is in force. We also note that the need to change the Board's composition was signalled early in the governance review and that preparatory work on derogation applications can commence in advance of the board's appointment.
- In regard to point h), the guidance will be published for consultation shortly after the decision on the licence modifications. It will be designed to assist SONI in making a derogation application but the fact that it is not yet published does not hinder SONI in considering Condition 42. Indeed, the work by SONI in preparatory steps for a derogation application may assist SONI to make a more meaningful and informed contribution to the consultation on the guidance.
- The limitations of timeframes proposed by UR for implementation (point i) are considered at 3.60 above and in Annex 3.
- In regard to point j), SONI should factor in existing and planned work streams (including SEMC and energy strategy related work streams) into its assessment of what initial derogations it wishes to apply for. SONI's arguments as to the need for a derogation in light of planned and current workstreams are factors which would be considered in any derogation application. The subsequent derogation process recognises that things may change over time and is sufficiently flexible to accommodate the uncertainty of future change as it includes a

provision allowing UR to bring forward any date in Part D (Paragraph 42). We have also made a drafting change to clarify how UR will exercise the power to vary time periods (see 4.37 below).

### ***Understated cost impact of the UR proposals***

High level points

3.62 SONI makes the following high points on the cost impact of UR's proposals:

- UR has failed to fully assess the effect of its proposals:
  - ◆ Provided only a high level set of assumptions, therefore UR's CBA is flawed and misleading. SONI considers that the costs associated with the UR's proposals will be substantial due to the impact SONI argues our proposals could have on a range of TSO functions.
  - ◆ UR retains full discretion as to what derogations to grant.
  - ◆ UR has the information to assess the potential ramifications on costs of unwinding of the integrated arrangements in place. Through the price review processes UR has visibility of, not only SONI TSO but also SEMO and SEMOpx, cost sharing and costs allocations. Also the total resources (all island) and costs and the allocation of those resources/costs between the TSOs was provided to the UR by SONI in 2017 to facilitate the operation of the revised SEM arrangements.
- Integration with EirGrid has benefit and cannot be replicated through the derogation process. The licence modifications will undo these benefits.

### ***IT systems impact***

3.63 SONI is also concerned about the impact of UR's proposals on IT systems. For example:

- ◆ The implementation of the UR proposals would result in separation of IT systems, processes and resources at a potentially much higher cost than is presented in the Licence Modifications Consultation and that cannot be addressed/mitigated through the proposed derogation process.
- ◆ The derogation process will result in conflicts with existing licence obligations (e.g. CRM auction provisions).

- ◆ The derogation process implies that UR has the vires to include additional conditions on SONI which could result in UR adding to, replacing, removing or altering existing SEMC decisions pertaining to shared integrated systems.
- ◆ Proposals cannot, if implemented, meet the 'vision' set out by UR for SONI independence.

3.64 SONI makes the following key points about the separation of IT systems, processes and resources:

- Due to level of IT integration SONI has been able to obtain substantial synergies from operating as part of the EirGrid Group. The ISEM is on the basis of the integrated model (determined by SEMC) and funding was approved by UR.
- The shared resources model impacts not only SONI TSO but also EirGrid TSO, SEMO and SEMOpx.
- SONI estimates that full system separation would cost in excess of £100m and take 8-10 years and in doing so would increase consumer bills by £7 to £8 per annum. SONI considers that these costs cannot be addressed/mitigated through the proposed derogation process.
- Also SONI states that 'regardless of the scale of derogations, there will be significant changes need to the existing IT arrangements as a result of the UR proposals.'<sup>73</sup>

### ***Cost allocation and recharges***

3.65 SONI states that UR has not addressed any queries to SONI on its regulatory accounts and refutes the risk that UR has identified that customers could be overcharged as well as the reference to hidden cross-subsidies.

3.66 SONI also considers the specific points made by UR on cost allocation and recharges and provides some further information on these specific costs, what they relate to, and the extent to which regulatory approvals were attached to these. For example:

- The £17m net transfer (£68M - £51M) of costs in 2018 was attributable to IT costs associated with I-SEM and rebalancing of generator charges.

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<sup>73</sup> See Paragraph 4.31 of the SONI response.

- The £2m swing in management charge over time was discussed with the UR during the price control process.
- 'Other costs' include costs relating to IT maintenance contracts, insurance and professional fees as well as including costs incurred in relation to the preparation of the SONI price control.
- Reflecting on the scale of the purchases and sales SONI notes that the I- SEM project was a key driver together with rebalancing of generator charges and the consequent impact on the G-TUoS<sup>74</sup> recharges. SONI has followed the cost allocation policy for the ISEM project as approved by the SEMC and the costs are based on UR approvals. Also, in SONI's view the allocation of costs is not open to management discretion but rather is strictly down to the Group allocation methodology.

3.67 SONI believes that UR's view that the manner in which the consideration of value or cost to NI consumers is taken into account is not transparent, and the claim that SONI is obliged to accept costs allocated by EirGrid to NI consumers is factually inaccurate and misrepresents the licence structures in place. SONI notes that:

*'Neither SONI, nor EirGrid through SONI, can allocate a charge to the Northern Ireland consumers. The decision as to what costs are ultimately approved and thus charged to consumers is a matter for the UR. This is undertaken on an annual basis via the tariff process.'*<sup>75</sup>

#### ***Impact on consumer bills***

3.68 SONI notes that it has not undertaken a full business assessment but has detailed the potential IT systems and resources in Annex 6 of its response. Consequently, SONI believes that UR has significantly understated the costs (£1.8m) in its CBA. Instead SONI has estimated that the impact of the UR proposals will increase annual domestic customer bills by approximately £7.00 – £8.00 and that this may cost domestic customers in the region of an additional £80 over the lifetime of the investment. This compares to the SONI price control 2020-2025, which increased domestic annual customer bills by an estimated £0.91 (based on the current arrangements).

#### ***SONI points related to UR's CBA***

3.69 As noted at 3.62 above SONI consider that UR's CBA is flawed and misleading as UR provided only a high level set of assumptions and the cost

<sup>74</sup> Transmission Use of System (TUoS) charges are levied on both suppliers and generators and are called G-TUoS in the case of generators.

<sup>75</sup> SONI response, Paragraph 4.41.

impact of UR's proposals will be substantial.

3.70 SONI also makes a number of specific points related to UR's CBA. For example SONI states that:

- No benefits have been set out by UR in terms of its actions;
- No consideration has been given to the costs required for the implementation of alternate arrangements / non-integrated arrangements where a derogation is not sought or not granted;
- No consideration has been given to the additional costs on EirGrid, SEMO and SEMOpx as applicable, for the preparation and ongoing management of derogations and Service Level Agreements ('SLAs') and how these will be recovered;
- The proposed forecast costs do not account for any travel costs that may be incurred if board members are European based;
- Where a derogation is rejected UR would need to provide SONI with, at a minimum, the necessary revenues and time to implement separation of the systems and/or services; and
- UR has not stated its assumptions or included costs in relation to additional activities that would fall to SONI under the proposed arrangements (preparation of derogation applications and the development and introduction of SLAs and the associated management and governance of these (from an EirGrid perspective).

### ***UR response***

#### ***UR response – SONI high level points***

- 3.71 We do not agree that UR has failed to fully assess the effect of our proposals. UR's CBA is based on the additional costs of implementing the new SONI board and new governance mechanisms. Any future costs will not be known until the derogation process has been undertaken and it is not possible to make an estimate at this stage. See 3.60 which addresses the future cost impact of UR's proposals. Also our response below to SONI's points on IT systems impact.
- 3.72 It is SONI's belief that UR proposals are based on an assumption that SONI will seek derogations in relation to all existing areas where any synergies or efficiencies are realised. That being the case SONI considers that UR will need to grant all such derogation requests absent the imposition of any conditions. It is for SONI to consider what derogations to apply for and to



substantiate the benefits that integration brings to NI consumers. We have made no assumptions in this regard, but given the statements already made by SONI in regard to the benefits of integration with EirGrid it is reasonable to assume that SONI will apply for a range of derogations.

- 3.73 In regard to SONI's view that UR retains full discretion as to what derogations to grant, we note that SEMC may call in any decision on a derogation application it considers to be a SEM matter.
- 3.74 In regard to SONI's view that UR has the information to assess the potential ramifications on costs of unwinding of the integrated arrangements in place – we note that we do not have information on EirGrid TSO costs as these are regulated by CRU and significant elements of SONI TSO's costs result from cost allocation to SONI of Group project or costs.
- 3.75 We do not agree that the benefits from integration with EirGrid cannot be replicated through the derogation process. The derogation process is designed to capture these benefits for NI customers but in a more transparent way than at present.

#### ***UR response - IT systems impact***

- 3.76 We acknowledge that independence from EirGrid Group companies is the default position in the new licence condition. However, we also wish to permit appropriate synergies and efficiencies that stem from SONI's position as part of the EirGrid Group<sup>76</sup>. Consequently, the new condition makes provision for derogations where benefits to consumers can be demonstrated. However, SONI's approach to the derogation process, and to its estimate of costs arising from the derogation process (both in section 4 and its case studies) seems predicated on full independence and no derogations being sought/allowed across a wide range of TSO functions. Such a position seems highly improbable given SONI TSO's consistent claims that integration has driven efficiency, resilience and security.
- 3.77 In regard to the likelihood that the additional IT costs SONI has identified will materialise, it is not possible to pre-empt the outcome of the derogation process now. However, we note that UR has placed no limits on the derogations that could be granted. UR will grant derogations to allow IT to continue to be integrated with EirGrid where SONI can make an evidenced case for this in line with the licence requirements. Also, the counterfactual costs of IT separation and exactly why it is not possible to separate some system without separating others could be relied on by SONI as part of its

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<sup>76</sup> See UR description of fit for purpose governance arrangements set out in the Call for Evidence (Paragraph 1.2)

case for derogation.

- 3.78 As stated above, we do not agree that the benefits from integration with EirGrid cannot be replicated through the derogation process. As noted above (3.51) SONI has not explained why there would be an impact on the SEM even where UR provided a derogation (or derogations) to SONI to continue to use, e.g. combined tools, particularly as a derogation could allow operation as at present. Consequently, SONI's case on cost impacts appears exaggerated.
- 3.79 In addition for the reasons set out in Annex 3 we do not agree that there is any conflict between Condition 42 and SONI TSO's existing licence conditions.
- 3.80 Also in regard to SONI's view that UR may not have the vires to impose additional conditions on SONI which add to, replace, remove or alter existing SEMC decisions pertaining to shared integrated systems – we note that SEMC may call-in any decision on a derogation application it considers to be a SEM matter (including a decision on any applicable conditions).

***UR response – cost allocation and recharges***

- 3.81 The additional information SONI has provided on recharges is helpful but has arisen in consequence of the governance review. As noted above at 2.44, due to the limited role of the SONI board in financial matters UR has no confidence that cross-business charging is being adequately scrutinised by SONI. For example, SONI partly attributes the scale of recharges to rebalancing of generator charges through G-TUoS tariffs. However, for the reasons explained in Annex 7, in the approach to G-TUoS charging SONI's governance structures were not such as to bring SONI to proactively address a unjustified difference in treatment of internal costs which had resulted in a disadvantageous situation for NI stakeholders.
- 3.82 It remains the case that the costs referred to were not allocated under a cost allocation and recharge policy approved by an independent SONI Board. UR's governance proposals will provide confidence that cost allocation and recharges to and from SONI and EirGrid in future are fully transparent and subject to scrutiny in SONI and accountability by SONI and if necessary challenge by SONI.
- 3.83 SONI's view is that neither SONI, nor EirGrid through SONI, can allocate a charge to the NI consumers and that the decision as to what costs are ultimately approved and thus charged to consumers is a matter for UR via the tariff process. It is the case that tariff approvals are a matter for UR. However, these decisions are dependent upon the reporting of actual spend, much of which results from cost allocations to SONI TSO for joint services

systems etc. Charges faced by NI consumers are heavily reliant on cost allocations between TSO's being undertaken in a fair and transparent manner. As explained above, UR considers that these cost allocations between TSOs are not presently transparent. An integral part of the responsibility of SONI TSO is to review and challenge these cost allocations. To say that cost allocations are a matter for UR misses the point: a reason for the licence modification is to ensure that there is transparency in the allocation of costs between TSOs so that UR can regulate effectively.

***UR response – impact on consumer bills***

- 3.84 For the reasons set out above we consider that SONI's case on cost impacts appears exaggerated, therefore we do not agree that our proposals will have the impact on consumer's bills which SONI claims.

***UR response - SONI points related to UR's CBA***

- 3.85 We do not agree that UR's CBA is flawed – see 3.85 above.

- 3.86 In regard to the specific points made by SONI related to UR's CBA:

- The April 2021 paper listed a number of potential benefits under the new arrangements including; a) challenge or rejection of Group costs by SONI; b) removal of 'one-size-fits-all' approach; and c) distinct service needs being developed by SONI. We consider those benefits to continue to hold good. SONI's response does not recognise that these benefits are legitimate, because it considers the interest of the NI consumer is by definition met by the current integrated arrangements with EirGrid plc.
- In regard to potential additional costs on EirGrid, SEMO and SEMOpx as applicable, for the preparation and ongoing management of derogations and SLAs, the CBA has made full provision for both the preparation of derogations and ongoing management of SLAs. This cost will be rightly incurred by SONI and represents typical project management arrangements when procuring services from an external body. It is notable that SONI itself argued for such an approach to vendor management in its 2020-25 business plan.<sup>77</sup> If such an approach is deemed correct for external contractors, it would also seem

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<sup>77</sup> As set out in Appendix D of the business plan this included:

- Establishing a simple charter for vendor management;
- Increased visibility into external spending;
- Collect and catalogue vendor contracts;
- Publish basic rules of engagement; and
- Develop performance standards for vendors.

reasonable when outsourcing work to EirGrid. It will be for other parties to decide if they wish to replicate these arrangements if availing of SONI expertise. These costs would however need to be covered by the relevant party.

- It is possible that some costs will be imposed on EirGrid with respect to compliance with SLA arrangements such as cost reporting. However, SONI has confirmed during the price control review process that much of this work is already undertaken as part of the normal cost allocation process / reviews (as is should be). Furthermore, it would be anticipated that a prudent operator would wish to know the costs and quality of services it purchases or delivers. Consequently, it is our assumption that much of the evidence already exists and any cost impact would be limited. Indeed, it is only if such matters are neither analysed, documented or tested – in other words simply approached on the basis of regular generic assumption – that there is work of any materiality to be done. The fact that such work is required is, if anything, itself a substantial potential cause for concern.
- In relation to SONI's concerns about the necessary revenues and time to implement separation of the systems and/or services, we note that the licence condition makes provision for additional time (12 months) to become compliant following a derogation decision. It also makes provision for a 6 month period to become compliant should a derogation be revoked. If SONI consider that such decisions will result in the imposition of additional cost, they can make such a case via the usual uncertainty mechanism arrangements. These requests will be considered accordingly.
- UR's assumptions in respect of additional costs associated with the preparation of derogation applications, SLAs, and the associated management and governance of these clearly stated in the April 2021 consultation document. SONI has not set out why it considers that these cost activities are underestimated. The assumptions for management costs can be summarised as follows:
  - ◆ **£50k** for one off recruitment costs for a Chair, three NEDs and three new staff members;
  - ◆ **£40k p.a.** for an independent Chair [an allowance materially above the €21.6k remuneration for the EirGrid Chairperson in 2021];

- ◆ **£20k p.a.** each for 3 Non-Executive Directors [an allowance materially above the €12.6k remuneration for the EirGrid NEDs in 2021];
  - ◆ **£91k p.a.** for a new Compliance Manager (even though UR do not consider this a full-time requirement and the relevant person will be free to work on other issues); and
  - ◆ **£79k p.a.** for two new analysts to construct derogation requests and subsequently assist with ongoing review and scrutiny of costs and quality of services in SONI, including those allocated from elsewhere in the Group under the SLA's.
- SONI is correct in its view that these costs will be dependent on the number of derogations and their ongoing management.
  - Allowances provided for the independent Chairperson and NEDs are in excess of what is currently awarded to EirGrid comparators. UR is of the opinion that the cost forecasts in the CBA adequately provide for any travel expenses, whether European based or otherwise.
  - As discussed in 3.60 above, additional costs may be incurred as a consequence of the derogation process, e.g. where a derogation is sought but not granted or alternative conditions are imposed. These future costs cannot and will not be known until the derogation process has been undertaken. It is therefore not possible to make an estimate at this stage.

3.87 Therefore UR does not consider that there is any error or failing in its cost benefit analysis (CBA) as set out in April 2021.

#### ***SONI response to the proposed licence modifications***

3.88 The following are the broad themes in SONI's response to licence condition 42. See Annex 3 for a more detailed summary.

- The drafting potentially overrules SEMC decisions and network code obligations and allows UR to add additional/different unspecified conditions.
- Contradictions/conflicts with existing licence conditions and no assessment of this as part of the reasons and effects section of the consultation. UR has not proposed any modifications to the existing conditions to address these.
- UR has delegated many of the proposed changes to guidance or future potential modifications. As such, SONI is unable to assess the

effects of the modifications proposed. SONI would have expected UR to have assessed the impact of its proposals against all licence conditions.

- The role of the parent company and shareholder in relation to amendment of SONI's 'articles of association'.
- Lack of published guidance documentation means that SONI cannot undertake a full assessment of the impact of the proposed modifications. This leaves SONI having to consider how the licence modifications will work as abstract concepts without any substantive guidance as to how they will operate in practice.
- Hard coded dates may penalise SONI if UR delays its decision. Further, by binding itself to these dates, UR risks undermining the consultation itself should they prove unworkable.
- There are no definitions for "Compliance Plan" and "Compliance Manager" and it is unclear how this drafting aligns with Condition 12 of the SONI TSO Licence.

### ***UR response***

3.89 The following is a summary of UR's response to the broad themes in SONI's response on Condition 42. See Annex 3 for a more complete UR response to the issues raised.

- The licence conditions provide for future decisions to be taken on derogations. These decisions may also be taken by SEMC as a SEM matter as necessary, including the specification of conditions.
- In Annex 3 we have assessed each instance where SONI considers it has identified a contradiction or conflict but find no issues to answer.
- We have not delegated 'proposed changes to guidance or future potential modifications'. The Guidance will be designed to assist SONI in making a derogation application. Future decisions will be taken as part of the derogation decision and these cannot be pre-empted now in advance of the evidence to support them becoming available.
- The proposals can legally be implemented in accordance with Irish law once the consent of the Minister is obtained. See 3.30 above.
- The Guidance will be published in due course but the fact that it is not yet published does not hinder SONI in considering Condition 42.
- We have added 5 months to the implementation dates specified in

Part D. The reason for this is to reflect the change in UR's timetable and thereby maintain the implementation periods allowed to SONI in the modification consulted on. Also, and for the reasons explained in section 4, we have also added a self-modification provision in the condition which would have the effect that the dates in Condition 42 are automatically changed such that SONI is not disadvantaged in any way in the event of an appeal to the CMA.

- For clarity we have included two new definitions – ‘Compliance Manager’ and ‘Compliance Plan’. Condition 12 requirements have a different purpose and therefore the two sets of requirements are distinct and each standalone.

## **Key points from the other responses**

3.90 All seven of the other responses received were supportive of the overall aims of UR in seeking changes to governance of SONI and acknowledged the need for SONI's TSO business to be led by a board and senior management focused on delivering NI's energy policy, and meeting its needs. Of those seven respondents:

- Five of those respondents agreed with the selection of “Option C”, albeit one of those would rather have seen a fully independent SONI (Option D). This includes the overwhelming support from the workforce of SONI for Option C with 82% of respondents supporting the proposed licence changes – as is apparent from a union survey of that workforce. Option C presumes SONI will be a standalone company independent of EirGrid unless an independent SONI Board can make an evidenced case to Utility Regulator to permit sharing of resources with EirGrid.
- One would have preferred “Option B”, which has an independent SONI Board and Management, but presumes that SONI will continue to deliver its TSO obligations through EirGrid's integrated management structure. This party acknowledged that derogations (where the SONI Board can make an evidenced case to Utility Regulator to permit sharing of resources with EirGrid) could allow the actual governance of SONI under option “C” to approach that under Option “B”.

3.91 As well as supporting UR's policy for the governance of SONI, the individual respondents made a number of specific points relating to the need for, and nature of, the proposed changes to SONI Governance. The key such comments are summarised in the following Paragraphs, grouped into the following areas:

- The need for change;



- The quality of work to date;
- The UK Corporate Governance Code (UKCGC);
- The role of derogations and compliance; and
- The makeup and appointment of the SONI Board.

### ***Need for Change***

3.92 In addition to being supportive of the changes to SONI Governance, some respondents went further in emphasising why that change is needed. Relevant comments include:

- Many respondents noted the importance of an accountable and transparent SONI at a time of significant change in the electricity industry paradigm. Two respondents went further, and noted that an NI focused SONI Board and management team will increase the chances of delivering the NI energy strategy vision. Both these parties are active members of the energy sector in NI, with one noting a potential lack of joined up thinking and common objectives across the SONI/EirGrid organisation.
- One party noted a specific case where SONI and EirGrid's operational interventions lacked transparency, and may not have balanced the interests of customers in NI with those in Republic of Ireland. It is implicit that this party suspects a different set of interventions would result where a meaningfully independent SONI must work alongside EirGrid in line with all the measures proposed by UR.

### ***Quality of work to date***

3.93 Two respondents noted the well-researched and thorough nature of UR's work to date on SONI Governance, including its consideration of the needs of NI consumers, and the emerging NI energy policy.

### ***UK Corporate Governance Code (UKCGC)***

3.94 A number of parties commented on the use of the UK Corporate Governance Code to inform UR's proposed licence changes. Comments in this area include those summarised below:

- UKCGC represents best practice for a regulated approach to balanced corporate governance. UR's proposed licence changes move SONI towards that best practice.

- UKCGC principles for the division of board responsibilities are consistent with the need for SONI to adopt a more transparent and accountable organisation structure, that better balances proportionate alignment between subsidiary and parent company, with a clear delineation of responsibility, assurance, accountability and strategy between SONI and EirGrid leadership.
- No one should fear transparency, accountability and independence. This creates confidence from consumers, who pay for the entire market.

### ***Role of Derogations and compliance***

3.95 Three respondents made comments relating to the inclusion of derogations within the UR proposals, as well as measuring compliance against the new licence conditions:

- One party stated that any derogation will need to be supported by robust evidence – to ensure transparency and positive evidence-based outcomes for NI consumers.
- One party expressed a concern that SONI may prevaricate through the derogations process, and then operate in a way that stretches or exceeds the bounds of any eventual derogation. This party suggests their concern is supported by the reluctance of SONI/EirGrid to engage constructively with UR relating to these governance proposals over the last 3 years. Given this concern, this party believes that effective policing of any compliance plan will be essential.
- One party was concerned that the processes of seeking derogations could be overly onerous and restrictive on SONI, and take management time that could be better spent elsewhere. This party expressed a desire for clear guidance on what would constitute an acceptable case for a derogation.

### ***Make up and appointment of the SONI Board***

3.96 A number of respondents made specific points relating to the make-up and appointment of the SONI board. Key points are summarised below:

- Two parties explicitly expressed support for the SONI Board to have a majority of sufficiently independent non-executive directors. One of these parties went further, stating there should be at least 3 independent directors.

- One party would have preferred a fully independent SONI Board, but acknowledged the right of EirGrid (as sole shareholder) to be represented on the SONI Board.
- One party stated the desire for an employee representative to be included on the SONI Board, and concern that this may be precluded by the proposed licence changes.
- Two parties expressed an opinion on UR being able to veto appointments to the SONI Board. One of these respondents supported this proposal, with the other being against. The respondent that opposes the UR veto does acknowledge benefits to UR having a collaborative role in the appointments process.
- One party noted an inconsistency in the proposals relating to the initial appointment of the SONI Board, with references to the Board being appointed by SONI, as well as references to the Board being appointed by an independent body.
- One party suggested that licence references for “decisions” taken by “managers” should be subject to a materiality threshold – to avoid it applying to all decisions

### ***UR response***

- 3.97 We note the level of support for UR’s licence changes and the rationale behind them from a wide range of stakeholders, including CCNI and SONI employees via the Prospect response. CCNI’s view on how SONI’s governance should be structured aligns well with that of UR:

*‘It remains our belief that, to best serve NI consumers, SONI should adopt a more transparent and accountable organisation structure, that better balances proportionate alignment between subsidiary and parent company, with a clear delineation of responsibility, assurance, accountability and strategic focus between SONI and EirGrid leadership.’*

- 3.98 This is also echoed in the MEL response:

*‘We support the requirements in the proposed licence changes for SONI to reform its governance structure so that it is independent, transparent, accountable, and focused on delivering and protecting the needs of Northern Ireland consumers.’*

- 3.99 We note that the Prospect response states a preference that derogations should be for relatively limited exceptions while the NIE Networks response expresses the opposite view – that the default of separate resourcing could have unintended and detrimental consequences. NIE Networks therefore asks that UR is pragmatic in its approach to derogation applications. As noted above, UR intends to exercise its discretion when dealing with

derogation requests in a pragmatic and cost-sensitive manner. But the evidential burden rests on SONI to substantiate the benefits of integration alongside its continued compatibility with the demands of the NI regulatory regime.

- 3.100 NIE Networks expressed a concern that the derogation process may be inflexible. UR's position is that in reality derogation applications may be made in respect of any business functions. There is also provision for subsequent derogation applications and we have made provision for flexibility in the timescales in respect of these (Condition 42, Paragraph 42).
- 3.101 The Prospect response asks that UR appoint a workforce representative to the SONI Board. A member of the SONI workforce sitting on the Board would not meet the definition of a Sufficiently Independent Director but that does not mean they could not sit on the Board or attend Board meetings in a different capacity. We note that the UKCGC expects boards to engage with the workforce but there are different ways of achieving this. Most boards have not chosen to do this with appointment of worker representatives to the board. We consider that it will be for the new independent SONI board to consider how best to engage with its workforce. In this regard the FRC has published work in this area which it may be helpful for SONI to consider.<sup>78</sup>

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<sup>78</sup> [FRC-Workforce-Engagement-Report\\_May-2021.pdf](#)

## 4. Summary of decision on the licence modifications

- 4.1 The statutory consultation published in January 2022 proposed modifications to SONI TSO licence by way of included a new condition, Condition 42: Governance and Management of the Licensee.

### *Responses received on the proposed new licence condition*

- 4.2 We have carefully considered the representations received in response to the statutory consultation. The specific points made by respondents and UR's response to them are summarised in section 3 and in more detail in respect of the SONI and EirGrid responses at Annexes 3 and 4 respectively.
- 4.3 None of the respondents suggested any changes to the drafting to implement UR's decision. The comments on the drafting related to aspects of the decision itself.
- 4.4 We are proceeding to modify the SONI TSO Licence to include the new condition largely as proposed in the statutory consultation. However, we have made some changes to the consultation version. Some of the changes address and respond to consultees' general comments on the licence condition, while others are made for the purposes of ensuring clarity of, and consistency in, the legal drafting. This section explains the relevant changes (other minor drafting changes have also been made and all of the changes can be seen in the marked-up of Condition 42 at Annex 1).

## SONI Board Composition

### *Part A: SONI Board*

- 4.5 Part A of the licence condition makes provision for the composition and functions of the board of SONI Limited (the **Board**). Among other things the new provisions include new requirements on Board composition and skill set, a definition of Sufficiently Independent Director (SID), matters for which the Board must be responsible, and terms of appointment for SIDs. The reasons and effects of the proposed licence condition were set out in Paragraphs 7.2-7.4 of the January licence modification consultation and continue to be applicable.

### *Changes to Part A post consultation*

#### ***Board appointment deadline (Paragraph 1)***

- 4.6 We have altered the date by which the new SONI board is to be appointed from 1 January 2023 to 1 June 2023. This change (and corresponding changes to other dates in the licence) essentially takes into account the fact that UR's timetable for making its final decision has changed from the timetable that was in contemplation at the time of the statutory consultation and consequentially pushes back the relevant date by the equivalent period. It also maintains a transition period providing SONI with sufficient time to undertake the process of recruiting/appointing the Board in compliance with licence requirements.

***Number of Experiences SIDs (Paragraph 5)***

- 4.7 We have amended the requirements with regard to the proportion of SIDs (from within the overall number) that should have prior TSO or energy industry related experience and the proportion that should have prior experience of working at senior level in the energy industry.
- 4.8 The reason for these changes is to ensure that the 'prior experience' requirements can be 'mathematically' satisfied whatever the overall composition of the Board may be (noting that the majority has to be SIDs).

***Length of Board Appointments (Paragraph 6)***

- 4.9 We have amended the requirement relating to the initial term of appointment for a sufficiently independent non-executive director from needing to be between 4 to 6 years to being between 3 and 6 years. We have also decided that there is no need to specify the minimum and maximum period for any second term of appointment – but retained the provision that cumulative period for any such director may not be more than 9 years.
- 4.10 The reason for these changes is to provide SONI with greater flexibility as to the lengths of Board appointments such that it can manage, as appropriate, the need for appointments to be staggered and achieve an effective balance of continuity of, and changes to, the composite Board.

***Information on Board appointment (Paragraph 10(b))***

- 4.11 We have amended the drafting so that UR may specify a date by which SONI must provide UR with information on intended appointees. This will ensure that UR has information and it may be considered in good time.
- 4.12 We have also clarified the legal drafting with regard to UR's ability to direct SONI not to make an appointment where to do so would otherwise lead to a breach of one or more of the other applicable requirements.

***Voting (Paragraph 12(b))***

- 4.13 We have strengthened the requirements with regards to voting rights to ensure that the weighting of votes cannot be structured in such a way as to circumvent or negate the other requirements relating to the composition of the Board.

***Matters reserved (Paragraph 14)***

- 4.14 We have made some additions to Paragraphs 14(b), (d), (f) and (g) in order to clarify the scope and extent of the matters which must be reserved to the Board, including in particular to require the Board to approve supporting documents in respect of any derogation application, matters relating to the appointment of the Compliance Manager, and the Compliance Plan.

***The Articles of Association (Paragraph 16)***

- 4.15 The Principal Obligation, relating to the specific requirements which are to be met in respect of the composition of the Board, is a 'best endeavours' obligation. This recognises the possibility that events may arise which are outside the control of the licensee, e.g. the number of applications it receives in response to its well-advertised recruitment process may be beyond its control, as it seeks to meet the obligation by the specified date.
- 4.16 However, we consider that the requirement on SONI to ensure the modification of its Articles of Association should be an absolute obligation rather than being subject to best endeavours. UR recognises that under Irish legislation Ministerial consent is required for to SONI's Articles of Association to be amended. However, UR is not aware of any reason as to why such Ministerial consent cannot or should not (a) be sought by EirGrid as provided for under the relevant legislation, and (b) be given in circumstances where any changes that may need to be made to the Articles of Association are for the purposes of making them consistent, and to facilitate compliance, with the licence condition requirements.

## **Managerial and Operational Independence**

***Part B: Operational Independence***

- 4.17 Part B of the licence condition relates to the separation of the SONI TSO business from EirGrid and any other company within the EirGrid Group.
- 4.18 The overall effect of this part of the licence is that, except in respect of those functions for which a derogation has been granted the SONI TSO business will need to be managerially and operationally separate from EirGrid and any other company within the EirGrid Group. Among other things the new



provisions include a definition of Separate Management and Separate Resources. The reasons and effects of the proposed licence condition were set out in Paragraphs 7.6-7.10 of the January licence modification consultation and continue to be relevant.

### ***Changes to Part B post consultation***

#### ***Effective date (Paragraphs 20(b))***

- 4.19 We have added five months to the date by which Business Functions which are not the subject of a derogation application, must be carried out by Separate Management and Separate Resources. The reason for this is to reflect the change in the UR's timetable and thereby maintain the implementation period which was proposed to be allowed to SONI in the modification consulted on.

#### ***Condition 42 (Paragraph 22(c))***

- 4.20 The definition of 'Separate Resources' among other things limits the data that SONI can share with EirGrid where a derogation is not in effect, to data sharing which is provided for in the SOA. SONI's response notes that it is unclear how this drafting interacts with the requirements under Condition 11 and in particular Paragraphs 4(c) and 4(d) of that Condition.
- 4.21 We have therefore made a drafting change to Condition 42 para 22(c) to make it clearer that where a derogation is not in place, any data sharing between SONI and EirGrid (and/or any other Associated Company) shall be in accordance with the terms of the SOA and that those terms shall reflect the requirements of Condition 11(4)(d). This means that data can be shared where the SOA provides for that to be the case and where that is otherwise permitted under Condition 11(4)(d). It is of course open to SONI to seek derogations to enable it to share data, in respect of any Business Function, which it would not otherwise be permitted to share under and in accordance with this provision.

### ***Part C: Initial Derogations***

- 4.22 While the principal obligation is that the SONI TSO business is to be managerially and operationally separate from EirGrid, Parts C and D of the proposed licence condition provide for the TSO business to be exempt from that requirement in respect of those business functions for which it has been given a derogation by UR.
- 4.23 Part C of the proposed licence condition therefore sets out the process, and associated timings, by which SONI may, in respect of any particular function(s), initially apply for derogation(s) from the requirement for the SONI

TSO business to be operationally separate from EirGrid and any other company within the EirGrid Group. The reasons and effects of the proposed licence condition were set out in Paragraphs 7.13-7.14 of the January licence modification consultation and continue to be relevant.

### ***Changes to Part C post consultation***

#### **Implementation dates (Paragraphs 24 and 27)**

- 4.24 We have added five months to the implementation dates specified in Part C. As above, the reason for this is to reflect the change in the UR's timetable and thereby maintain the implementation periods proposed to be allowed to SONI in the modification consulted on.

#### ***Content of derogation application (Paragraphs 25(c)-(f))***

- 4.25 Paragraph 25 includes requirements that SONI must meet in respect of any application for a derogation. We have made a number of changes to Paragraph 25 to ensure clarity as to the derogation application requirements in the licence.
- 4.26 In Paragraph 25(c) we have added drafting the effect of which is to ensure that where a Services Agreement is proposed by SONI as part of any arrangements for management or resources to be shared in common with other companies in the EirGrid Group, that the terms of any proposed Services Agreement are included in the derogation application. The reason for this is to ensure the all supporting information and documents are included within the application.
- 4.27 In Paragraph 25(d) we have added drafting that encourages SONI to include in a derogation application any conditions to which SONI considers a derogation should be subject. SONI's response expressed concern at the fact that the licence condition allow UR to attach conditions to the grant of a derogation. The reason for (and effect of) the changed drafting is to encourage SONI to frame potential conditions in its application so that SONI's views on potential conditions may be considered by UR at the outset.
- 4.28 We have amended Paragraph 25(e) to make reference to the statutory duties of the Authority as set out in the Principles and Guidance on Condition 42 Derogations<sup>79</sup> (rather than referring to Article 12 of the Energy Order specifically on the face of the licence). The reason for this is that SONI's response expressed a concern at the drafting of this sub-paragraph and we acknowledge that the original reference to Article 12 alone may not be correct given that an application for a derogation could be considered by the

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<sup>79</sup> UR may issue this guidance document under Condition 42, Paragraph 36.

SEMC as a SEM matter.

- 4.29 Furthermore when making an application, SONI will not know whether its application will be decided by the SEMC or by the UR Board. Therefore we propose that the specific statutory duties together with guidance on matters that may be relevant for UR consideration and for SEMC consideration are set out in the Principles and Guidance document a draft of which will be published for consultation following the decision on the licence modifications. We will liaise with the SEMC to obtain its input and sign off on in respect of the principles and guidance that it proposes for any applications which may be decided upon by the SEMC, i.e. where it has determined it to be a SEM matter.
- 4.30 We have also included (as new Paragraph 25(f)) a requirement for the derogation application to be made in accordance with any procedural requirements that may be specified in the Principles and Guidance document. This is essentially to clarify that there will be important procedural requirements with regard to derogation applications specified in that document which must be complied with if an application is to be treated as valid.

***Invalid Applications (Paragraph 26)***

- 4.31 Additional drafting has been included in this Paragraph to provide that SONI will get a notification where a derogation application does not meet the requirements on timings and content and is therefore deemed to be invalid. The reason for this is to clarify that SONI will know when its application is deemed invalid.

***Applications deemed granted (Paragraph 28 and Paragraph 45)***

- 4.32 Paragraph 28 (and Paragraph 45 in Part D) provides that if UR has not determined an initial derogation application by the dates set out in Paragraph 27, the application shall be deemed to be granted. However, it was silent on the period of time for which the derogation is granted. We have therefore added drafting to Paragraph 28 to provide that any application deemed to be granted under Paragraph 28 will be time limited for five years.<sup>80</sup> Also, we have added drafting to clarify that the application will be deemed granted in respect of any Business Function and any conditions, as may have been set out in SONI's original application for derogation.

***Derogation Expiry Date (Paragraph 31 and 32(a))***

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<sup>80</sup> Similarly, Paragraph 31 has been amended to clarify that any 'formally' granted derogation will be time limited - not less than five years but could be for a longer period. See also the amendment at Paragraph 45 in respect of applications for subsequent derogations which are deemed granted.

- 4.33 The consultation draft provided that a derogation granted by UR could include a condition as to the length of the derogation. On reflection UR has decided that all derogations granted will be given for a specific period (always for at least five years) and then expire if not renewed on a further application. The reason for the change is to ensure greater clarity and consistency by confirming that all derogations will have an expiry date, and to require all existing derogations to be subject to review after a suitable period before they can be continued.

***Consultation on Principles and Guidance document (Paragraph 36)***

- 4.34 We have made a drafting change to Paragraph 36 to clarify that the ‘Principles and Guidance on Condition 42 Derogations’ will be issued following consultation with the licensee and any other person UR considers appropriate.<sup>81</sup> We have also added a provision for the Principles and Guidance document to include procedural requirements to be followed by SONI in respect of an application for derogation.

***Part D: Subsequent derogations***

- 4.35 Part D of the licence condition sets out the process and timings for SONI to be able to apply for a derogation at a later stage, i.e. essentially after 1 December 2028. The reasons and effects of the proposed licence condition were set out in Paragraphs 7.16-7.17 of the January licence modification consultation and continue to be relevant.

***Changes to Part D post consultation***

***Implementation Timings/Dates (Paragraphs 37, 38, and 39)***

- 4.36 We have added five months to the dates specified in Part D. The reason for this is to reflect the change in UR's timetable and thereby maintain the implementation periods allowed to SONI in the modification consulted on.

***Variation of Time (Paragraphs 42 and 43)***

- 4.37 In its response SONI commented that all the dates in Condition 42 were (as it describes it) ‘hard coded’. That is not actually correct in regard to the subsequent derogation process as Paragraph 42 allows UR to vary any date or period of time specified in Part D so as to bring it forward. However, for clarity we have made a drafting change by the incorporation of a new Paragraph 43 to make it clear that the power to change dates may be exercised in a targeted fashion in relation to specific business functions and particular circumstances (such as where something, for instance the law, has changed). Paragraph 42 also now makes clear that it is applicable only in

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<sup>81</sup> This includes the SEMC.

respect of the Business Function that is specified in any direction given.

## **Compliance Plan**

- 4.38 Part E of the licence condition replicates many of the existing provisions for SONI to prepare and report on a compliance plan that are contained in Condition 12. The reasons and effects of Part E in the proposed licence condition were set out in Paragraphs 7.19-7.20 of the January licence modification consultation and continue to be relevant.

### ***Changes to Part E post consultation***

- 4.39 We have adjusted the date by which SONI is required to submit the first compliance plan under Condition 42 from 1 January 2023 to 1 December 2023.<sup>82</sup> The revised date falls after the latest date for submission of derogation applications. The reason for this change is to permit the new independent SONI Board the opportunity to review and approve the compliance plan, including SONI's plans to ensure compliance with the requirements for Separate Management and Separate Resources in respect of any business functions where it did not apply for a derogation from the Principal Obligation in Part B.
- 4.40 We have added a reference to 'monitoring' in Paragraph 55(d). This makes it clear that the duties and tasks of the Compliance Manager will also include recommending and advising on remedial action (as necessary) following monitoring work by the Compliance Manager. The reason for the change is to ensure consistency with the duties of the Compliance Manager following any investigation work.

## **Other changes to the licence modifications**

### ***Part F***

- 4.41 A new Part F has been added to Condition 42 which provides for any date specified in the new Condition 42 to be pushed back by seven months in circumstances where the licence modification does not come into effect on the date specified by the UR pursuant to Article 14(9) of the Order because of an ongoing appeal to the CMA in respect of that decision and in the event that the appeal is ultimately disallowed by the CMA. This will ensure that, in such circumstances, SONI has the same amount of time to implement and comply with the licence requirements as it has should the licence modifications come into effect on the date specified by the UR under Article

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<sup>82</sup> This can be seen in Paragraph 46 with a consequential amendment at Paragraph 51.

14(9) of the Order.

### ***Definitions***

- 4.42 Three new definitions have been added to Part G – Compliance Manager, Compliance Plan, and Modification Decision. These are included within Part G essentially for clarification purposes only (the terms were defined in the consultation draft but not within Part G itself). The definition of Related Undertaking has been removed as this term is already defined in Condition 1(8) of the licence.

### **Decision on the licence modifications**

- 4.43 Our final decision on the licence modifications to the SONI TSO licence to give effect to governance changes are set out in Annex 1.

## 5. Conclusions and next steps

### Principles and Guidance document

- 5.1 As noted in Paragraph 4.34 above, the Principles and Guidance on Condition 42 Derogations will be published for consultation following the decision on the licence modifications. We will liaise with the SEMC in respect of the Principles and Guidance that it proposes for any applications which may be decided upon by the SEMC, i.e. where it has determined an application for a derogation to be a SEM matter.

### Interaction between the derogation process and price control

- 5.2 SONI considers that UR's proposals lead to a clear requirement for a new price control to be developed to reflect the proposed arrangements and ensure that SONI has the resources required in order to meet all of its obligations and that the associated risks and financing needs are fully considered. We do not agree that a new price control is needed.
- 5.3 However, applications for derogations are required by 30 November 2023 with decisions to be made by 1 June 2024 – 1 December 2024. Therefore, any derogation decisions will fall to be implemented either just prior to the end of the 2020-2025 price control period or at the very beginning of the next price control period.
- 5.4 In the case of derogation decisions which must be implemented by SONI between April and September 2025, any claims for additional allowances can and will be considered as part of the uncertainty mechanism process. Derogation decisions which fall to be implemented after 1 October 2025 and any implications flowing from them can be either taken account of in the price control decisions related to the 2025-2030 price control or future uncertainty mechanism applications/decisions.<sup>83</sup>
- 5.5 Similarly, where business functions are not subject to a derogation decision and must be separated from EirGrid this must be done by 1 December 2024 any claims for additional allowances can and will be considered as part of

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<sup>83</sup> EirGrid's response (Paragraph 85) stated that a recovery mechanism for additional unforeseen costs to EirGrid and SEMO will need to be determined and assumes that it is NI consumers who will bear any additional costs. If any cross-subsidisation is revealed between EirGrid and SONI then this will need to be unwound and dealt with in the relevant price control and who will bear any costs will be determined by the nature of the cross subsidy. If the derogation process otherwise results in separation between SONI and EirGrid or SEMO then this will indicate that there are benefits to de-integration and the costs of achieving that will need to be considered in the context of the benefits to consumers.



the uncertainty mechanism process.

- 5.6 Work on the next SONI price control would expect to commence in late 2023 with a business plan submission by SONI TSO in the late spring/early summer of 2024. Therefore, SONI will know what derogations it has applied for several months in advance of making its business plan submission. SONI can therefore base the plan on the derogations for which it has applied.
- 5.7 Derogation decisions will have been made before UR publishes the draft determination for the price control, and so any implications flowing from them can be taken into account by UR in the draft and final determinations.
- 5.8 In the event of an appeal to the CMA which confirms the UR's licence modification decision, all derogation decisions would fall to be implemented in the 2025-2030 price control period and any implications flowing from them can be taken account of in the price control decisions related to that control.

# Annex 1: Final licence modifications to implement governance changes

## Condition 42. Governance and Management of the Licensee

### INTRODUCTION

1. This condition makes provision for the effective corporate governance and management of the Licensee in the interests of consumers, and consists of seven parts:
  - (a) **Part A** makes provision for the composition and functioning of the board of directors of the Licensee;
  - (b) **Part B** requires that the management and resources used by the Licensee for the purposes of the Transmission System Operator Business are those which are dedicated to the Licensee alone;
  - (c) **Part C** makes provision for the Licensee to apply for, and the Authority to be able to issue initial, derogations from the requirements of Part B in respect of one or more designated business functions of the Licensee;
  - (d) **Part D** makes provision for the Licensee to apply for further derogations in the future where it did not do so initially, where its initial applications were rejected, or where any derogations that were granted have been revoked or are due to expire;
  - (e) **Part E** requires the Licensee to adopt a compliance plan and appoint a compliance manager to ensure that it complies with the requirements of this condition;
  - (f) **Part F** makes provision for this condition to be modified in the manner specified in that Part; and
  - (g) **Part G** sets out various defined terms which are relevant to this condition.

## PART A. THE BOARD OF THE LICENSEE

### The Principal Obligation

2. The Licensee must take all steps within its power to ensure that, with effect from 1 June 2023 and at all times after that date, the board of the Licensee is constituted and operates in accordance with the first to the thirteenth requirements of this Part A.

### The Specific Requirements

3. The **first** requirement is that a majority of the directors of the Licensee must be Sufficiently-Independent Directors.
4. The **second** requirement is that, the chair of the board of the Licensee must be a Sufficiently-Independent Director.
5. The **third** requirement is that, of the Sufficiently-Independent Directors on the board of the Licensee at any time:
  - (a) at least one-quarter must be individuals who, at the time of their respective initial appointments to that role, had substantial and recent experience of working:
    - (i) at senior level in, or for, a European Electricity Transmission System Operator; or
    - (ii) in, or for, a part of the European Energy Industry in a capacity which required them to have routine engagement at senior level with a European Electricity Transmission System Operator; and
  - (b) at least one-half (to include all individuals satisfying the requirement of sub-paragraph (a), who shall be treated as also satisfying the requirement of this sub-paragraph (b)) must be individuals who, at the time of their respective initial appointments to that role, had substantial and recent experience of working at senior level in, or for, a part of the European Energy Industry.

6. The **fourth** requirement is that each Sufficiently-Independent Director must be appointed for an initial term which is neither less than three years nor more than six years, and may be re-appointed on one occasion only so long as the aggregate period of both appointments does not exceed nine years.
7. The **fifth** requirement is that, in order to ensure continuity in the functioning of the board of the Licensee, the terms of appointment of the Sufficiently-Independent Directors must be staggered so that no more than one-third of those appointments are due to expire at the same time.
8. The **sixth** requirement is that:
  - (a) there must be no more than one Non-Executive Director on the board of the Licensee who is not a Sufficiently-Independent Director; and
  - (b) all other directors on the board who are not Sufficiently-Independent Directors must be Executive Directors.
9. The **seventh** requirement is that the membership of the board of the Licensee must reflect as a whole an appropriate mix and balance of skills, knowledge, experience and personal qualities necessary for ensuring the effective management and governance of the Licensee.
10. The **eighth** requirement is that, prior to the appointment of any director to the board of the Licensee:
  - (a) the Licensee must give written notice of the intended appointment to the Authority;
  - (b) the Licensee must provide to the Authority all information relating to the intended appointee that it may reasonably request, and do so by any such date as it may reasonably specify; and
  - (c) where - within 20 working days following the receipt of that notice or (if later) of such information and evidence as it has reasonably requested - the Authority concludes that the appointment would give rise to a breach of any one or more

of the first to the seventh requirements of this part and directs the Licensee to not make the appointment, the Licensee must not make the appointment.

11. The **ninth** requirement is that any meeting of the board of the Licensee must not be treated as quorate unless the majority of directors present and able to vote are Sufficiently-Independent Directors.
12. The **tenth** requirement is that, at a meeting of the board of the Licensee:
  - (a) no director of the Licensee may exercise more than one vote (or a vote weighted so as to be worth more than that of any other director) on any matter, except for the chair who, in any case where there is an equal number of votes, may be permitted to exercise a second and casting vote; and
  - (b) no director or category of directors may be required to have voted in favour of a resolution on any matter in order for it to be treated as passed, or to have voted against a resolution on any matter in order for it to be treated as rejected.
13. The **eleventh** requirement is that, where the chair of the board of the Licensee is unavoidably absent from any meeting of the board, that meeting must be chaired by another Sufficiently-Independent Director.
14. The **twelfth** requirement is that the matters which are reserved for a decision by the board of the Licensee must include at least the following:
  - (a) determining whether to make any application for a Derogation under Part C or D;
  - (b) approving the content of any such Derogation application, including the evidence and information provided in support of it, prior to its submission to the Authority;
  - (c) approving the terms of the System Operator Agreement and of any amendment to that agreement;
  - (d) making, and approving any revision to, any:

- (i) scheme of delegation of the Licensee that is concerned with the allocation of authority (so far as is permitted, consistently with this twelfth requirement) to members of the board, committees or employees of the Licensee to make decisions or exercise functions on behalf of the Licensee;
    - (ii) conflict of interest policy applicable to members of the board, committees or employees of the Licensee; and
    - (iii) whistleblower policy of the Licensee;
  - (e) approving the terms of any Services Agreement and of any amendment to any such agreement;
  - (f) approving the appointment of the Compliance Manager, any termination of that appointment by the Licensee, and (where the appointment is for a limited term) any decision by the Licensee not to renew or extend that appointment; and
  - (g) approving the terms of the Compliance Plan, of any proposal to revise the Compliance Plan, and of any revision of the Compliance Plan made after receiving a notification from the Authority specifying changes that are required to be made to it.
15. The **thirteenth** requirement is that no decisions relating to the business of the Licensee may be reserved to a vote of shareholders except those decisions in respect of which such a vote is required by or under the Companies Act 2006.

### **The Articles of Association**

16. The Licensee must, by no later than 1 June 2023, ensure the modification of the articles of association of the Licensee to such extent as is requisite or necessary to make them consistent, and secure that they facilitate compliance, with the first to the thirteenth requirements set out above.

### **Key Definition**

17. For the purposes of this condition, a **Sufficiently-Independent Director** means a natural person who is a director of the Licensee and who:
- (a) to the reasonable satisfaction of the Authority, has the skills, knowledge, experience and personal qualities necessary to perform that role effectively;
  - (b) has no executive responsibilities within the Licensee or any Associated Company;
  - (c) is not at any time during his appointment as a director of the Licensee, and was not at any time during the five years prior to that appointment:
    - (i) an employee of the Licensee;
    - (ii) an employee or director of any Associated Company; or
    - (iii) in any Material Business Relationship with the Licensee or any Associated Company;
  - (d) is not at any time during his appointment as a director of the Licensee a Close Relation of a person who is at the same time:
    - (i) an employee of the Licensee;
    - (ii) an employee of any Associated Company; or
    - (iii) in any Material Business Relationship with the Licensee or any Associated Company; and
  - (e) does not at any time during his appointment as a director of the Licensee:
    - (i) hold a remit to represent the interests of any particular shareholder or group of shareholders of the Licensee or of any Associated Company; or
    - (ii) receive remuneration from the Licensee or from any Associated Company other than a director's fee and reasonable expenses.



## PART B. MANAGERIAL AND RESOURCE SEPARATION

### The Principal Obligation

18. On and from the Effective Date, and at all times after that date, the Licensee must ensure that all activities carried out by it in the course of the Transmission System Operator Business are carried out by means of Separate Management and Separate Resources.

### The Exception

19. However, the principal obligation in this Part B shall not apply in respect of any Business Function to the extent that:
- (a) the Licensee has applied for, and been granted by the Authority, a Derogation under either Part C or Part D in relation to that Business Function; and
  - (b) the Derogation remains extant, having neither reached its Derogation Expiry Date nor been revoked by the Authority for material non-compliance by the Licensee with any of its conditions.

### Key Definitions

20. For the purposes of this condition, the **Effective Date** means:
- (a) where the Licensee has applied in accordance with Part C for a Derogation in respect of any one or more Business Functions, the date, in relation to each such Business Function, which falls twelve months after the Derogation Decision Date;
  - (b) in respect of all other Business Functions, 1 December 2024.
21. For the purposes of this condition, **Separate Management** means, in relation to activities carried out by the Licensee in the course of the Transmission System Operator Business, that all decisions relating to those activities are taken by managers who, at all levels (up to and including Executive Director) are:

- (a) employed by the Licensee;
  - (b) engaged solely in the management and operation of the Transmission System Operator Business; and
  - (c) not in an employment relationship with, engaged in providing services of any kind to, or otherwise subject to any other contractual or professional duties in respect of any Associated Company.
22. For the purposes of this condition, **Separate Resources** means, in relation to activities carried out by the Licensee in the course of the Transmission System Operator Business, that:
- (a) those activities are carried out using personnel who are:
    - (i) employed, or engaged under a contract of services, by the Licensee; and
    - (ii) not in an employment relationship with, engaged in providing services of any kind to, or otherwise subject to any other contractual or professional duties in respect of any Associated Company;
  - (b) those activities are carried out using managerial and operational resources – including in particular premises, IT and other systems, equipment, facilities, processes and tangible and intellectual property – which are not shared with or accessible to any Associated Company; and
  - (c) no data obtained or created in the course of carrying out the activities are shared with or accessible to any Associated Company other than on terms provided for in the System Operator Agreement which reflect and comply with the requirements of paragraph 4(d) of Condition 11 of the Licence.

## **PART C. APPLICATIONS FOR INITIAL DEROGATIONS**

### **Applications for a Derogation from Part B**

23. The Licensee may apply to the Authority for a direction that it is not required to comply with the principal obligation in Part B in relation to any one or more Business Functions, and for the purposes of this condition such a direction shall be known as a **Derogation**.

#### **Timing and Content of Application**

24. The Licensee may submit to the Authority an application for a Derogation under this Part C:
- (a) no earlier than 1 October 2023; and
  - (b) no later than 30 November 2023.
25. The Licensee must ensure that any application for a Derogation is made in writing, specifies clearly the Business Functions to which it relates, and separately in respect of each Business Function to which it relates:
- (a) describes in detail the activities which together constitute that Business Function;
  - (b) specifies the characteristics of the Shared Management and Shared Resources that the Licensee would propose to use, if the Derogation were granted, for the purposes of carrying out the activities falling within the description of that Business Function;
  - (c) sets out the arrangements with one or more Associated Companies by virtue of which that Shared Management and those Shared Resources would be used in common, including the terms of any proposed Services Agreement;
  - (d) sets out any conditions to which the Licensee considers that the Derogation, if it were granted, should be subject;
  - (e) states why, in the submission of the Licensee, the granting of a Derogation in relation to that Business Function would be best calculated to further the statutory duties of the Authority referred to in the Principles and Guidance on Condition 42 Derogations, having regard to the other matters set out in that document;

- (f) is made in compliance with such procedural requirements as the Authority may specify in the Principles and Guidance on Condition 42 Derogations;
  - (g) includes such other information and evidence as may be required in accordance with the Principles and Guidance on Condition 42 Derogations, in such form and detail as may be set out in that document; and
  - (h) is accompanied by all other information and evidence that the Licensee wishes the Authority to take into account when considering the application.
26. Any application received by the Authority which does not meet these requirements on timing and content shall be deemed to be invalid and, subject only to the Licensee having received notification from the Authority of that invalidity, the provisions of this Condition 42 shall apply as if no such application had been made by the Licensee.

### **Consideration by the Authority**

#### *Timing*

27. The date by which the Authority is to determine any application for a Derogation shall be the later of:
- (a) 1 June 2024; or
  - (b) where, prior to 1 June 2024, the Authority is satisfied that it requires more time to consider the application, such alternative date as it may specify in a direction issued to the Licensee, save that:
    - (i) the Authority may issue no more than one such direction in respect of that application;
    - (ii) the latest date that may be specified in such a direction is 1 December 2024.
28. Where the Authority has not determined an application for a Derogation by the date identified in accordance with the previous paragraph:

- (a) the Derogation shall be deemed to be granted:
  - (i) by the Authority on that date; and
  - (ii) on the basis applied for by the Licensee, including (in particular) in respect of the Business Function described, and subject to any such conditions as may have been set out, in the Licensee's application for a Derogation;
- (b) the Derogation Expiry Date shall be the date which is five years from the Derogation Decision Date.

#### *Duty of the Licensee*

29. The Licensee must:

- (a) in good faith assist and co-operate with the Authority to such extent as the Authority may reasonably request in order to facilitate its consideration of any application for a Derogation; and
- (b) in particular provide to the Authority all further information and evidence that it may reasonably request for that purpose as soon as reasonably practicable after it is requested.

#### **Determination by the Authority**

30. The Authority may, having considered any application for a Derogation, in respect of each Business Function to which that application relates:

- (a) reject the application and decline to grant a Derogation;
- (b) grant a Derogation:
  - (i) in respect of that Business Function by reference to the activities described by the Licensee in its application; or

- (ii) in respect of such an amended description of the activities which constitute that Business Function as the Authority may specify in its determination.
- 31. A Derogation granted by the Authority shall specify the date on which it expires (the **Derogation Expiry Date**), save that this shall not be less than five years after the Derogation Decision Date.

#### *Conditions*

- 32. Where the Authority grants a Derogation, it may grant it subject to such conditions as it considers requisite or expedient, which may, in respect of any Business Function by reference to which the Derogation is granted, include in particular conditions:
  - (a) as to the circumstances in which, and restrictions subject to which, the Licensee may use Shared Management and Shared Resources for the purposes of carrying on the activities constituting that Business Function;
  - (b) specifying in respect of any Services Agreement in relation to Shared Management and Shared Resources used for the purposes of that Business Function, a requirement to enter into that agreement on such terms as may be:
    - (i) specified in the condition; or
    - (ii) determined, or subject to approval, by the Authority in accordance with any process which may be set out in the condition;
  - (c) making such provision as the Authority considers appropriate to secure the effective ring-fencing of any Shared Management and Shared Resources which may be used for the purpose of that Business Function from all Separate Management and Separate Resources required under this condition to be used for that, or any other, Business Function; and
  - (d) containing provision for any of those conditions, or any such parts of them as may be specified, to have effect and/or cease to have effect on and from:
    - (i) such date as may be specified in the condition;

- (ii) such date as may be determined by the Authority in accordance with any process which may be set out in the condition; or
  - (iii) the occurrence of such event or existence of such circumstances as may be described in the condition.
- 33. The Licensee must comply with the requirements of any conditions to which a Derogation is subject.
- 34. Where the Authority determines that the Licensee is in material non-compliance with any conditions of a Derogation, it may:
  - (a) at any time amend the Derogation by attaching to it such further or modified conditions as it considers requisite or expedient; or
  - (b) revoke the Derogation on a date prior to its Derogation Expiry Date, so long as the Authority gives to the Licensee no less than six months' notice prior to that revocation becoming effective (the **Derogation Revocation Date**).
- 35. The Authority may, on the request of the Licensee, at any time amend the conditions to which a Derogation is subject in such manner as the Licensee has requested and to which the Authority has consented.

### **The Principles and Guidance on Condition 42 Derogations**

- 36. The Authority may following consultation with the Licensee and such other persons as it considers appropriate, issue, and from time to time amend, a document which shall be known as the **Principles and Guidance on Condition 42 Derogations**, which may set out:
  - (a) guidance as to the process to be followed by the Authority in considering applications for Derogations under Part C or Part D;
  - (b) guidance as to the statutory duties to be followed by the Authority and the principles to be applied by it when deciding whether or not, and subject to what conditions, to grant a Derogation under Part C or Part D; and



- (c) requirements as to:
  - (i) the form and content of the information and evidence which must be provided by the Licensee as part of any application for a Derogation under Part C or Part D; and
  - (ii) the procedure be followed by the Licensee in respect of that application.

## **PART D. SUBSEQUENT APPLICATIONS FOR DEROGATIONS**

### **Applications which may be Made under this Part D**

#### *First-Time Applications*

- 37. Where, in relation to any Business Function, the Licensee did not apply for a Derogation under Part C by 30 November 2023, it may apply for a Derogation in relation to that Business Function under this Part D on a date which is no earlier than 1 December 2028.

#### *Originally Invalid Applications*

- 38. Where, in relation to any Business Function, the Licensee applied for a Derogation under Part C by 30 November 2023, but the application was treated as invalid for non-compliance with the requirements of Part C, the Licensee may apply for a Derogation in relation to the same Business Function under this Part D on a date which is no earlier than 1 December 2028.

#### *Originally Rejected Applications*

- 39. Where, in relation to any Business Function, the Licensee applied for a Derogation under Part C by 30 November 2023, and the application was rejected by the Authority, the Licensee may apply for a Derogation in relation to the same Business Function under this Part D on a date which is no earlier than five years after the Derogation Decision Date.

#### *Originally Granted Applications – Revocation of Derogation*

40. Where, in relation to any Business Function, the Licensee applied for and was granted a Derogation under Part C, but that Derogation was later revoked by the Authority for a material non-compliance by the Licensee with its conditions, the Licensee may apply for a Derogation in relation to the same Business Function under this Part D on a date which is no earlier than five years after the Derogation Revocation Date.

#### *Originally Granted Applications – Expiry of Derogation*

41. Where, in relation to any Business Function, the Licensee applied for and was granted (or deemed to have been granted) a Derogation under Part C, the Licensee may apply for a Derogation in relation to the same Business Function under this Part D on a date which is no earlier than two years prior to the Derogation Expiry Date.

#### *Variation of Time*

42. The Authority may, by a direction issued to the Licensee, modify any date or period of time specified in any of the preceding paragraphs of this Part D, but that direction:
- (a) may only have the effect for the purpose of bringing forward that date or shortening that period of time to such extent as it may specify; and
  - (b) may be limited to applying only in respect of such Business Function as it may identify.
43. In any direction issued under the preceding paragraph, the Authority may specify limitations on the purpose for which the date or period of time is to be brought forward or shortened – including (in particular) limitations designed to restrict any new application for a Derogation to addressing only the consequences of such change of law or of circumstance as the direction may describe – in which case the Licensee may make any new application for a Derogation in accordance with the date or period of time specified in the direction only to the extent that it complies with such limitations.

#### **Applicability of Part C**

44. Where the Licensee is entitled to make an application for a Derogation under this Part D, the provisions of Part C shall apply to it in full, in the same way as if it had been an

application made under that Part, except that in substitution for the corresponding provisions of Part C:

- (a) the earliest date at which an application may be made shall be the one specified in accordance with, and subject to any limitations imposed by, the proceeding provisions of this Part D;
- (b) there shall be no latest date by which an application may be made; and
- (c) the date by which the Authority is to determine any application for a Derogation shall be the later of:
  - (i) the date which falls six months after the application was received by it; or
  - (ii) where, prior to the expiry of that six month period, the Authority is satisfied that it requires more time to consider the application, such alternative date as it may specify in a direction issued to the Licensee, save that:
    - (A) the Authority may issue no more than one such direction; and
    - (B) the latest date that may be specified by the Authority in any such direction is the date which falls twelve months after the application was received by it.

45. In the same manner as in Part C, where the Authority has not determined an application for a Derogation by the date identified in accordance with the previous paragraph, the Derogation shall be deemed to be granted by the Authority on that date on the basis applied for by the Licensee and the Derogation Expiry Date shall be the date which is five years from the Derogation Decision Date.

## **PART E. FACILITATING AND MONITORING COMPLIANCE**

### **The Compliance Plan**

46. The Licensee must, by no later than 1 December 2023, prepare and submit to the Authority a draft plan, which shall:
- (a) set out the practices, procedures, systems and rules of conduct which the Licensee has adopted, or intends to adopt, together with the timescales for adoption, to ensure its compliance with the requirements of this condition; and
  - (b) require to be approved by the Authority (and following such approval shall be known for the purposes of this condition as the **Compliance Plan**).
47. The Licensee must take all steps within its power to comply with its Compliance Plan and shall publish the up to date Compliance Plan on its website.
48. The Licensee must submit any proposed revisions to the Compliance Plan to the Authority for its approval, and those revisions may not be made until the Authority has approved them.
49. The Authority may:
- (a) within 30 days of the Licensee submitting an initial draft plan or a revised Compliance Plan; or
  - (b) following any review of the Compliance Plan that the Authority may conduct from time to time,

notify the Licensee that, in its opinion, the draft plan is not, or the Compliance Plan is no longer, suitable for the purpose of ensuring the Licensee's compliance with the requirements of this condition, and specify such revisions which must be made to it as are in the Authority's opinion necessary or expedient in order for it to be appropriate for that purpose and capable of approval by the Authority.

50. Where the Licensee receives such a notification, it shall within 30 days revise the draft plan or the Compliance Plan (as the case may be) in such manner and to such extent as is necessary to reflect the Authority's requirements.
51. The Licensee shall review the Compliance Plan on at least an annual basis so as to ensure that the Compliance Plan is accurate and up-to-date and remains suitable for

the purpose of ensuring the Licensee's compliance with the requirements of this condition.

52. The Licensee must ensure that all persons who from time to time are engaged in the management and operation of the Transmission System Operator Business:
- (a) are made aware of the practices, procedures, systems and rules of conduct set out in the Compliance Plan;
  - (b) have the necessary information and facilities to comply with their respective obligations under the Compliance Plan; and
  - (c) are aware of the disciplinary procedures that may be activated should they fail to comply with their obligations under the Compliance Plan.

### **The Compliance Manager**

53. The Licensee, following consultation with the Authority, must ensure that there is at all times a senior employee engaged in the management of the Transmission System Operator Business who is appointed to a role which has the purpose of facilitating compliance with its obligations under this condition and with the Compliance Plan, and that person shall be known for the purposes of this condition as the **Compliance Manager**.
54. The Licensee shall ensure that the Compliance Manager has access to such staff, premises, systems, information, documentation, equipment, facilities and other resources as he might reasonably expect to require to fulfil the duties and tasks assigned to him.
55. The duties and tasks which the Licensee assigns to the Compliance Manager must include:
- (a) providing relevant advice and information to the Licensee for the purpose of ensuring its compliance with this Condition and with the Compliance Plan;
  - (b) monitoring the effectiveness of, and the Licensee's compliance with, the Compliance Plan;

- (c) investigating any complaint or representation received by the Licensee from any person in respect of any matter arising under or by virtue of this condition or in relation to the Compliance Plan;
- (d) recommending and advising upon the remedial action which any such monitoring or investigation has demonstrated to be necessary or desirable, including where necessary revising the Compliance Plan to reflect such recommendation and advice; and
- (e) reporting regularly – at least annually, or with such greater frequency as the board of the Licensee may require or as may be specified in a notice issued by the Authority to the Licensee from time to time – to the directors of the Licensee on:
  - (i) His activities during the period covered by the report;
  - (ii) The outcome of any investigations he has conducted during that period; and
  - (iii) On his assessment of the Licensee’s compliance with this condition and with the Compliance Plan, clearly identifying any areas of non-compliance that he has identified and the remedial actions required in order to address them.

56. The Licensee must ensure that the Authority promptly receives a copy of each report that is given by the Compliance Manager to the directors of the Licensee.

## PART F – MODIFICATION OF RELEVANT DATE

57. This Part F applies where an application has been made for an appeal to be brought under Article 14B of the Order against the decision by the Authority to modify the conditions of the Licence to include this Condition 42 (the **Modification Decision**), and the CMA has:

- (a) granted permission for the bringing of the appeal;
- (b) given a direction pursuant to paragraph 1 of Schedule 5A of the Order; and

(c) confirmed the Modification Decision.

58. Where this Part F applies, this condition is modified such that each date specified in it by virtue of the Modification Decision is amended so as to be the date which falls seven months' later than was specified by virtue of that decision.

## **PART G. DEFINITIONS**

59. For the purposes of this condition:

### **Associated Company**

means any company which is:

- (a) part of the EirGrid Group, but excluding the Licensee itself; and
- (b) (if not part of the EirGrid Group) an affiliate, related undertaking or ultimate controller of the Licensee.

### **Business Function**

means a set of activities carried on by the Licensee for the purposes of the Transmission System Operator Business which:

- (a) in the context of an application made by the Licensee for a Derogation, are as described by the Licensee in that application; and
- (b) in the context of any Derogation granted by the Authority following such an application, are as described by the Authority in that Derogation.

### **Close Relation**

means, in relation to an individual, another individual who is their spouse (or partner of



equivalent nature), parent, child, sibling, grandparent or grandchild.

**Compliance Manager** has the meaning given to that expression in paragraph 53.

**Compliance Plan** has the meaning given to that expression in paragraph 46.

**Derogation** has the meaning given to that expression in paragraph 23.

**Derogation Decision Date** means, in relation to any application for a Derogation made by the Licensee under Part C or Part D:

- (a) the date on which the Authority notifies the Licensee of its decision either to grant or reject that application ; or
- (b) where either paragraph 28 or 45 applies, the date on which a Derogation is deemed to have been granted.

**Derogation Expiry Date** has the meaning given to that expression in paragraph 31.

**Derogation Revocation Date** has the meaning given to that expression in paragraph 34.

**Effective Date** has the meaning given to that expression in paragraph 20.

**EirGrid Group** means EirGrid plc, each of its affiliates and

	Related Undertakings, and each company for which EirGrid plc or one of its affiliates or Related Undertakings is a holding company.
<b>European Electricity Transmission System Operator</b>	means an entity which acts (or at any time acted) as electricity transmission system operator in any part of the United Kingdom, or any member state of the European Union or the European Free Trade Area.
<b>European Energy Industry</b>	<p>comprises those entities engaged in carrying out the activities of:</p> <ul style="list-style-type: none"> <li>(a) the generation, transmission, distribution and supply of electricity; and</li> <li>(b) the storage, and the conveyance, shipping and supply through pipes, of natural gas,</li> </ul> <p>any part of the United Kingdom, or any member state of the European Union or the European Free Trade Area.</p>
<b>Executive Director</b>	means a director of the Licensee who is also an employee of the Licensee.
<b>Material Business Relationship</b>	<p>means any material business relationship between an individual and an entity, including in particular a relationship in which the individual acts as a provider of professional or consultancy services, or is involved in the supply of any other goods or services, to that entity, but shall not include (taken by itself):</p> <ul style="list-style-type: none"> <li>(a) the holding by an individual of a small number of shares or associated rights in</li> </ul>

the Licensee or any Associated Company;  
or

- (b) the receipt by an individual of any pension or other accrued benefit associated with prior employment or service with the Licensee or any Associated Company.

**Modification Decision** has the meaning given to that expression in paragraph 57.

**Non-Executive Director** means a director of the Licensee who is not an Executive Director.

**Principles and Guidance on Condition 42 Derogations** has the meaning given to that expression in paragraph 36.

**Separate Management** has the meaning given to that expression in paragraph 21.

**Separate Resources** has the meaning given to that expression in paragraph 22.

**Services Agreement** means an agreement (whether or not legally-binding) between the Licensee and any Associated Company which relates to the provision or staff or other resources by the Licensee to that company, or by that company to the Licensee, or any sharing of staff or other resources between the Licensee and that company.

**Shared Management** means managerial staff taking decisions in relation to activities carried out by the Licensee in the course of the Transmission

System Operator Business which do not constitute Separate Management.

**Shared Resources**

means resources used in relation to activities carried out by the Licensee in the course of the Transmission System Operator Business which do not take the form of Separate Resources.

**Sufficiently-Independent  
Director**

has the meaning given to that expression in paragraph 17.

## **Condition 42. Governance and Management of the Licensee**

### **INTRODUCTION**

1. This condition makes provision for the effective corporate governance and management of the Licensee in the interests of consumers, and consists of ~~six~~seven parts:
  - (a) **Part A** makes provision for the composition and functioning of the board of directors of the Licensee;
  - (b) **Part B** requires that the management and resources used by the Licensee for the purposes of the Transmission System Operator Business are those which are dedicated to the Licensee alone;
  - (c) **Part C** makes provision for the Licensee to apply for, and the Authority to be able to issue initial, derogations from the requirements of Part B in respect of one or more designated business functions of the Licensee;
  - (d) **Part D** makes provision for the Licensee to apply for further derogations in the future where it did not do so initially, where its initial applications were rejected, or where any derogations that were granted have been revoked or are due to expire;
  - (e) **Part E** requires the Licensee to adopt a compliance plan and appoint a compliance manager to ensure that it complies with the requirements of this condition; ~~and~~
  - (f) **Part F** makes provision for this condition to be modified in the manner specified in that Part; and
  - (g) **Part G** sets out various defined terms which are relevant to this condition.

## PART A. THE BOARD OF THE LICENSEE

### The Principal Obligation

2. The Licensee must take all steps within its power to ensure that, with effect from 1 ~~January~~ June 2023 and at all times after that date, the board of the Licensee is constituted and operates in accordance with the ~~first to the thirteenth~~ requirements of this Part A.

### The Specific Requirements

3. The **first** requirement is that, ~~at all times,~~ a majority of the directors of the Licensee must be Sufficiently-Independent Directors.
4. The **second** requirement is that, ~~at all times,~~ the chair of the board of the Licensee must be a Sufficiently-Independent Director.
5. The **third** requirement is that, ~~at all times~~ of the Sufficiently-Independent Directors on the board of the Licensee at any time:
  - (a) at least one ~~half of the Sufficiently-Independent Directors on the board of the Licensee~~ quarter must be individuals who, at the time of their respective initial appointments to that role, had substantial and recent experience of working: ~~at senior level in, or for, a part of the European Energy Industry; and~~
  - ~~(b) — from within those referred to in paragraph (a), at least one-quarter of the Sufficiently-Independent Directors on the board of the Licensee must be individuals who, at the time of their respective appointments to that role, had substantial and recent experience of working:~~
    - (i) at senior level in, or for, a European Electricity Transmission System Operator; or
    - (ii) ~~in, or for, a part of the European Energy Industry~~ in a capacity which required them to have routine engagement at senior level with a European Electricity Transmission System Operator; ~~and~~

- (b) at least one-half (to include all individuals satisfying the requirement of sub-paragraph (a), who shall be treated as also satisfying the requirement of this sub-paragraph (b)) must be individuals who, at the time of their respective initial appointments to that role, had substantial and recent experience of working at senior level in, or for, a part of the European Energy Industry.
6. The **fourth** requirement is that each Sufficiently-Independent Director must be appointed for ~~aan initial~~ term which is neither less than ~~fourthree~~ years nor more than six years, and may be re-appointed on one occasion only ~~for a term which is also neither less than four years nor more than six years, but~~ so long as the aggregate period of both appointments does not exceed nine years.
7. The **fifth** requirement is that, in order to ensure continuity in the functioning of the board of the Licensee, the terms of appointment of the Sufficiently-Independent Directors must be staggered so that no more than one-third of those appointments are due to expire at the same time.
8. The **sixth** requirement is that, ~~at all times~~:
- (b) there must be no more than one Non-Executive Director on the board of the Licensee who is not a Sufficiently-Independent Director; and
- (c) all other directors on the board who are not Sufficiently-Independent Directors must be Executive Directors.
9. The **seventh** requirement is that the membership of the board of the Licensee must, ~~at all times~~, reflect as a whole an appropriate mix and balance of skills, knowledge, experience and personal qualities necessary for ensuring the effective management and governance of the Licensee.
10. The **eighth** requirement is that, prior to the appointment of any director to the board of the Licensee:
- (a) the Licensee must give written notice of the intended appointment to the Authority, ~~and~~;



- (b) **the Licensee must** provide to the Authority all information relating to the intended appointee that it may reasonably request, **and do so by any such date as it may reasonably specify**; and
  - (c) where— within 20 working days following the receipt of that notice or (if later) of such information and evidence as it has reasonably requested — the Authority ~~notifies the Licensee that it has determined~~**concludes** that the appointment would give rise to a breach of any one or more of the first to the seventh requirements of this part, ~~that determination shall be treated as final and binding and~~**and directs the Licensee to not make the appointment**, the Licensee must not make the appointment.
- 11. The **ninth** requirement is that ~~neany~~ meeting of the board of the Licensee ~~may~~**must not** be treated as quorate unless the majority of directors present and able to vote are Sufficiently-Independent Directors.
- 12. The **tenth** requirement is that, **at a meeting of the board of the Licensee**:
  - (a) no director of the Licensee may exercise more than one vote (or a vote weighted so as to be worth more than that of any other director) on any ~~matter at a meeting of the board of the Licensee~~, except for the chair who, in any case where there is an equal number of votes, may be permitted to exercise a second and casting vote-; **and**
  - (b) **no director or category of directors may be required to have voted in favour of a resolution on any matter in order for it to be treated as passed, or to have voted against a resolution on any matter in order for it to be treated as rejected.**
- 13. The **eleventh** requirement is that, where the chair of the board of the Licensee is unavoidably absent from any meeting of the board, that meeting must be chaired by another Sufficiently-Independent Director.
- 14. The **twelfth** requirement is that the matters which are reserved for a decision by the board of the Licensee must include at least the following:
  - (a) determining whether to make any application for a Derogation under Part C or D;

- (b) approving the content of any such Derogation application ~~that it has determined to make, including the evidence and information provided in support of it, prior to its submission to the Authority;~~
- (c) approving the terms of the System Operator Agreement and of any amendment to that agreement;
- (d) making, and approving any revision to, any:
  - (i) scheme of delegation of the Licensee that is concerned with the allocation of authority (so far as is permitted, consistently with this twelfth requirement) to members of the board, committees or employees of the Licensee to make decisions or exercise functions on behalf of the Licensee;
  - (ii) conflict of interest policy applicable to members of the board, committees or employees of the Licensee; and
  - (iii) whistleblower policy of the Licensee;
- (e) approving the terms of any Services Agreement and of any amendment to any such agreement; ~~and~~
- (f) approving the appointment of the Compliance Manager, any termination of that appointment by the Licensee, and (where the appointment is for a limited term) any decision by the Licensee not to renew or extend that appointment; and
- (g) approving the terms of the Compliance Plan, of any proposal to revise the Compliance Plan, and of any revision of the Compliance Plan made after receiving a notification from the Authority specifying changes that are required to be made to it.

15. The **thirteenth** requirement is that no decisions relating to the business of the Licensee may be reserved to a vote of shareholders except those decisions in respect of which such a vote is required by or under the Companies Act 2006.

The ~~fourteenth~~ requirement is that the **Articles of Association**

16. The Licensee must, by no later than 1 June 2023, ensure the modification of the articles of association of the Licensee to such extent as is requisite or necessary to make them consistent, and secure that they facilitate compliance, with the first to the thirteenth requirements- set out above.

### Key Definition

17. For the purposes of this condition, a **Sufficiently-Independent Director** means a natural person who is a director of the Licensee and who:
- (a) to the reasonable satisfaction of the Authority, has the skills, knowledge, experience and personal qualities necessary to perform that role effectively;
  - (b) has no executive responsibilities within the Licensee or any Associated Company;
  - (c) is not at any time during his appointment as a director of the Licensee, and was not at any time during the five years prior to that appointment:
    - (i) an employee of the Licensee;
    - (ii) an employee or director of any Associated Company; or
    - (iii) in any Material Business Relationship with the Licensee or any Associated Company;
  - (d) is not at any time during his appointment as a director of the Licensee a Close Relation of a person who is at the same time:
    - (i) an employee of the Licensee;
    - (ii) an employee of any Associated Company; or
    - (iii) in any Material Business Relationship with the Licensee or any Associated Company; and
  - (e) does not at any time during his appointment as a director of the Licensee:

- (i) hold a remit to represent the interests of any particular shareholder or group of shareholders of the Licensee or of any Associated Company; or
- (ii) receive remuneration from the Licensee or from any Associated Company other than a director's fee and reasonable expenses.

## **PART B. MANAGERIAL AND RESOURCE SEPARATION**

### **The Principal Obligation**

18. On and from the Effective Date, and at all times after that date, the Licensee must ensure that all activities carried out by it in the course of the Transmission System Operator Business are carried out by means of Separate Management and Separate Resources.

### **The Exception**

19. However, the principal obligation in this Part B shall not apply in respect of any Business Function to the extent that:
- (a) the Licensee has applied for, and been granted by the Authority, a Derogation under **either** Part C or Part D in relation to that Business Function; and
  - (b) the Derogation remains extant, having neither reached its Derogation Expiry Date ~~(if any)~~ nor been revoked by the Authority for material non-compliance by the Licensee with any of its conditions.

### **Key Definitions**

20. For the purposes of this condition, the **Effective Date** means:
- (a) where the Licensee has applied in accordance with Part C for a Derogation in respect of any one or more Business Functions, the date, in relation to each such Business Function, which falls twelve months after the Derogation Decision Date;

- (b) in respect of all other Business Functions, 1 ~~July~~December 2024.
21. For the purposes of this condition, **Separate Management** means, in relation to activities carried out by the Licensee in the course of the Transmission System Operator Business, that all decisions relating to those activities are taken by managers who, at all levels (up to and including Executive Director) are:
- (a) employed by the Licensee;
  - (b) engaged solely in the management and operation of the Transmission System Operator Business; and
  - (c) not in an employment relationship with, engaged in providing services of any kind to, or otherwise subject to any other contractual or professional duties in respect of any Associated Company.
22. For the purposes of this condition, **Separate Resources** means, in relation to activities carried out by the Licensee in the course of the Transmission System Operator Business, that:
- (a) those activities are carried out using personnel who are:
    - (i) employed, or engaged under a contract of services, by the Licensee; and
    - (ii) not in an employment relationship with, engaged in providing services of any kind to, or otherwise subject to any other contractual or professional duties in respect of any Associated Company;
  - (b) those activities are carried out using managerial and operational resources – including in particular premises, IT and other systems, equipment, facilities, processes and tangible and intellectual property – which are not shared with or accessible to any Associated Company; and
  - (c) no data obtained or created in the course of carrying out the activities are shared with or accessible to any Associated Company other than on terms

provided for in the System Operator Agreement **which reflect and comply with the requirements of paragraph 4(d) of Condition 11 of the Licence.**

## **PART C. APPLICATIONS FOR INITIAL DEROGATIONS**

### **Applications for a Derogation from Part B**

23. The Licensee may apply to the Authority for a direction that it is not required to comply with the principal obligation in Part B in relation to any one or more Business Functions, and for the purposes of this condition such a direction shall be known as a **Derogation**.

### **Timing and Content of Application**

24. The Licensee may submit to the Authority an application for a Derogation under this Part C:
- (a) no earlier than 1 ~~May~~**October** 2023; and
  - (b) no later than 30 ~~June~~**November** 2023.
25. The Licensee must ensure that any application for a Derogation is made in writing, specifies clearly the Business Functions to which it relates, and separately in respect of each Business Function to which it relates:
- (a) describes in detail the activities which together constitute that Business Function;
  - (b) specifies the characteristics of the Shared Management and Shared Resources that the Licensee would propose to use, if the Derogation were granted, for the purposes of carrying out the activities falling within the description of that Business Function;
  - (c) sets out the arrangements with one or more Associated Companies by virtue of which that Shared Management and those Shared Resources would be used in common, **including the terms of any proposed Services Agreement**;

- (d) sets out any conditions to which the Licensee considers that the Derogation, if it were granted, should be subject;
  - (e) states why, in the submission of the Licensee, the granting of a Derogation in relation to that Business Function would be best calculated to further the ~~principal objective~~ statutory duties of the Authority ~~at Article 12 of~~ referred to in the ~~Energy Order~~ Principles and Guidance on Condition 42 Derogations, having regard to the other matters ~~referred to set out~~ in that ~~Article~~ document;
  - (f) is made in compliance with such procedural requirements as the Authority may specify in the Principles and Guidance on Condition 42 Derogations;
  - (g) includes such other information and evidence as may be required in accordance with the Principles and Guidance on Condition 42 Derogations, in such form and detail as may be set out in that document; and
  - (h) is accompanied by all other information and evidence that the Licensee wishes the Authority to take into account when considering the application.
26. Any application received by the Authority which does not meet these requirements on timing and content shall be deemed to be invalid and ~~rejected without further consideration~~, subject only to the Licensee having received notification from the Authority of that invalidity, the provisions of this Condition 42 shall apply as if no such application had been made by the Licensee.

## Consideration by the Authority

### *Timing*

27. The date by which the Authority is to determine any application for a Derogation shall be the later of:
- (a) 1 ~~January~~ June 2024; or
  - (b) where, prior to 1 ~~January~~ June 2024, the Authority is satisfied that it requires more time to consider the application, such alternative date as it may specify in a direction issued to the Licensee, save that:



- (i) the Authority may issue no more than one such direction **in respect of that application;**
  - (ii) the latest date that may be specified in such a direction is 1 **JulyDecember** 2024.
- 28. Where the Authority has not determined an application for a Derogation by the date identified in accordance with the previous paragraph, ~~the Derogation shall be deemed to be granted on that date on the basis applied for by the Licensee.:~~
  - (a) the Derogation shall be deemed to be granted:**
    - (i) by the Authority on that date; and**
    - (ii) on the basis applied for by the Licensee, including (in particular) in respect of the Business Function described, and subject to any such conditions as may have been set out, in the Licensee's application for a Derogation;**
  - (b) the Derogation Expiry Date shall be the date which is five years from the Derogation Decision Date.**

#### *Duty of the Licensee*

- 29. The Licensee must:
  - (a) in good faith assist and co-operate with the Authority to such extent as the Authority may reasonably request in order to facilitate its consideration of any application for a Derogation; and
  - (b) in particular provide to the Authority all further information and evidence that it may reasonably request for that purpose as soon as reasonably practicable after it is requested.

#### **Determination by the Authority**

30. The Authority may, having considered any application for a Derogation, in respect of each Business Function to which that application relates:
- (a) reject the application and decline to grant a Derogation;
  - (b) grant a Derogation:
    - (i) in respect of that Business Function by reference to the activities described by the Licensee in its application; or
    - (ii) in respect of such an amended description of the activities which constitute that Business Function as the Authority may specify in its determination.
31. A Derogation granted by the Authority shall specify the date on which it expires (the **Derogation Expiry Date**), save that this shall not be less than five years after the Derogation Decision Date.

#### *Conditions*

32. Where the Authority grants a Derogation, it may ~~attach~~ grant it subject to ~~it~~ such conditions as it considers requisite or expedient, which may, in respect of any Business Function by reference to which the Derogation is granted, include in particular conditions:
- ~~(a) as to the length of the period for which the Derogation is granted and the date on which it expires (the **Derogation Expiry Date**), save that this shall not be less than five years after the Derogation Decision Date;~~
  - (a) as to the circumstances in which, and restrictions subject to which, the Licensee may use Shared Management and Shared Resources for the purposes of carrying on the activities constituting that Business Function;
  - (b) specifying in respect of any Services Agreement in relation to Shared Management and Shared Resources used for the purposes of that Business Function, a requirement to enter into that agreement on such terms as may be:

- (i) specified in the condition; or
    - (ii) determined, or subject to approval, by the Authority in accordance with any process which may be set out in the condition;
  - (c) making such provision as the Authority considers appropriate to secure the effective ring-fencing of any Shared Management and Shared Resources which may be used for the purpose of that Business Function from all Separate Management and Separate Resources required under this condition to be used for that, or any other, Business Function; and
  - (d) containing provision for any of those conditions, or any such parts of them as may be specified, to have effect and/or cease to have effect on and from:
    - (i) such date as may be specified in the condition;
    - (ii) such date as may be determined by the Authority in accordance with any process which may be set out in the condition; or
    - (iii) the occurrence of such event or existence of such circumstances as may be described in the condition.
33. The Licensee must comply with the requirements of any conditions ~~to which are attached to~~ a Derogation ~~is subject~~.
34. Where the Authority determines that the Licensee is in material non-compliance with any conditions of a Derogation, it may:
- (a) at any time amend the Derogation by attaching to ~~it~~ such further ~~or modified~~ conditions as it considers requisite or expedient; or
  - (b) revoke the Derogation on a date prior to ~~any expiry date which may be specified in its conditions~~ **Derogation Expiry Date**, so long as the Authority gives to the Licensee no less than six months' notice prior to that revocation becoming effective (the **Derogation Revocation Date**).

35. The Authority may, on the request of the Licensee, at any time amend the conditions ~~attaching~~to which a Derogation is subject in such manner as the Licensee has requested and to which the Authority has consented.

### **The Principles and Guidance on Condition 42 Derogations**

36. The Authority may following consultation with the Licensee and such other persons as it considers appropriate, issue, and from time to time amend, a document which shall be known as the **Principles and Guidance on Condition 42 Derogations**, which may set out:
- (a) guidance as to the process to be followed by the Authority in considering applications for Derogations under Part C or Part D;
  - (b) guidance as to the statutory duties to be followed by the Authority and the principles to be applied by ~~the Authority~~it when deciding whether or not, and subject to what conditions, to grant a Derogation under Part C or Part D; and
  - (c) requirements as to:
    - (i) the form and content of the information and evidence which must be provided by the Licensee as part of any application for a Derogation under Part C or Part D; and
    - (ii) the procedure be followed by the Licensee in respect of that application.

## **PART D. SUBSEQUENT APPLICATIONS FOR DEROGATIONS**

### **Applications which may be Made under this Part D**

#### *First-Time Applications*

37. Where, in relation to any Business Function, the Licensee did not apply for a Derogation under Part C by 30 ~~June~~November 2023, it may apply for a Derogation in relation to ~~the same~~that Business Function under this Part D on a date which is no earlier than 1 ~~July~~December 2028.

### *Originally Invalid Applications*

38. Where, in relation to any Business Function, the Licensee applied for a Derogation under Part C by 30 ~~June~~November 2023, but the application was ~~treated as~~ invalid for non-compliance with the requirements of Part C ~~and therefore deemed under that Part to be rejected~~, the Licensee may apply for a Derogation in relation to the same Business Function under this Part D on a date which is no earlier than 1 ~~July~~December 2028.

### *Originally Rejected Applications*

39. Where, in relation to any Business Function, the Licensee applied for a Derogation under Part C by 30 ~~June~~November 2023, and the application was ~~treated as valid but was determined to be~~ rejected by the Authority, the Licensee may apply for a Derogation in relation to the same Business Function under this Part D on a date which is no earlier than five years after the Derogation Decision Date.

### *Originally Granted Applications – Revocation of Derogation*

40. Where, in relation to any Business Function, the Licensee applied for and was granted a Derogation under Part C, but that Derogation was later revoked by the Authority for a material non-compliance by the Licensee with its conditions, the Licensee may apply for a Derogation in relation to the same Business Function under this Part D on a date which is no earlier than five years after the Derogation Revocation Date.

### *Originally Granted Applications – Expiry of Derogation*

41. Where, in relation to any Business Function, the Licensee applied for and was granted ~~(or deemed to have been granted)~~ a Derogation under Part C, ~~but a condition was attached to that Derogation which specified that it was to expire on a certain date~~, the Licensee may apply for a Derogation in relation to the same Business Function under this Part D on a date which is no earlier than two years prior to the Derogation Expiry Date.

### *Variation of Time*

42. The Authority may, by a direction issued to the Licensee, modify any date or period of time specified in any of the preceding paragraphs of this Part D, but ~~only for the purpose of bringing forward that date or the date which is calculated by reference to that period of time.~~that direction:
- (a) ~~may only have the effect for the purpose of bringing forward that date or shortening that period of time to such extent as it may specify; and~~
  - (b) ~~may be limited to applying only in respect of such Business Function as it may identify.~~
43. ~~In any direction issued under the preceding paragraph, the Authority may specify limitations on the purpose for which the date or period of time is to be brought forward or shortened – including (in particular) limitations designed to restrict any new application for a Derogation to addressing only the consequences of such change of law or of circumstance as the direction may describe – in which case the Licensee may make any new application for a Derogation in accordance with the date or period of time specified in the direction only to the extent that it complies with such limitations.~~

### **Applicability of Part C**

44. Where the Licensee is entitled to make an application for a Derogation under this Part D, the provisions of Part C shall apply to it in full, in the same way as if it had been an application made under that Part, except that in substitution for the corresponding provisions of Part C:
- (a) the earliest date at which an application may be made shall be the one specified in ~~accordance with, and subject to any limitations imposed by,~~ the proceeding provisions of this Part D;
  - (b) there shall be no latest date by which an application may be made; and
  - (c) the date by which the Authority is to determine any application for a Derogation shall be the later of:
    - (i) the date which falls six months after the application was received by it;
    - or

(ii) where, prior to the expiry of that six month period, the Authority is satisfied that it requires more time to consider the application, such alternative date as it may specify in a direction issued to the Licensee, save that:

(C) the Authority may issue no more than one such direction; and

(D) the latest date that may be specified by the Authority in any such direction is the date which falls twelve months after the application was received by it.

45. In the same manner as in Part C, where the Authority has not determined an application for a Derogation by the date identified in accordance with the previous paragraph, the Derogation shall be deemed to be granted **by the Authority** on that date on the basis applied for by the Licensee **and the Derogation Expiry Date shall be the date which is five years from the Derogation Decision Date.**

## **PART E. ~~FACILITATING~~FACILITATING AND MONITORING COMPLIANCE**

### **The Compliance Plan**

46. The Licensee must, by no later than 1 ~~January~~**December** 2023, prepare and submit to the Authority a **draft** plan, which shall:

(a) set out the practices, procedures, systems and rules of conduct which the Licensee has adopted, or intends to adopt, together with the timescales for adoption, to ensure its compliance with the requirements of this condition; and

(b) require to be approved by the Authority~~;~~ (and following such approval shall be known for the purposes of this condition as the **Compliance Plan**~~;~~).

47. The Licensee must take all steps within its power to comply with its Compliance Plan and shall publish the up to date Compliance Plan on its website.

48. The Licensee must submit any proposed revisions to the Compliance Plan to the Authority for its approval, and those revisions may not be made until the Authority has approved them.



49. The Authority may:

- (a) within 30 days of the Licensee submitting an initial ~~draft plan~~ or a revised ~~plan~~ **Compliance Plan**; or
- (b) following any review of the Compliance Plan that the Authority may conduct from time to time,

notify the Licensee that, in its opinion, the ~~draft~~ plan is not, or the Compliance Plan is no longer, suitable for the purpose of ensuring the Licensee's compliance with the requirements of this condition, and specify such revisions which must be made to it as are in the Authority's opinion necessary or expedient in order for it to be appropriate for that purpose and capable of approval by the Authority.

50. Where the Licensee receives such a notification, it shall within 30 days revise the ~~plan~~ **draft plan or the Compliance Plan (as the case may be)** in such manner and to such extent as is necessary to reflect the Authority's requirements.

51. The Licensee shall review the Compliance Plan

~~(a) — by 1 July 2023; and~~

~~(b) on at least once in each subsequent period of twelve months,~~

**an annual basis** so as to ensure that the Compliance Plan is accurate and up-to-date and remains suitable for the purpose of ensuring the Licensee's compliance with the requirements of this condition.

52. The Licensee must ensure that all persons who from time to time are engaged in the management and operation of the Transmission System Operator Business:

- (a) are made aware of the practices, procedures, systems and rules of conduct set out in the Compliance Plan;
- (b) have the necessary information and facilities to comply with their respective obligations under the Compliance Plan; and

- (c) are aware of the disciplinary procedures that may be activated should they fail to comply with their obligations under the Compliance Plan.

### **The Compliance Manager**

- 53. The Licensee, following consultation with the Authority, must ensure that there is at all times a senior employee engaged in the management of the Transmission System Operator Business who is appointed to a role which has the purpose of facilitating compliance with its obligations under this condition and with the Compliance Plan, and that person shall be known for the purposes of this condition as the **Compliance Manager**.
- 54. The Licensee shall ensure that the Compliance Manager has access to such staff, premises, systems, information, documentation, equipment, facilities and other resources as he might reasonably expect to require to fulfil the duties and tasks assigned to him.
- 55. The duties and tasks which the Licensee assigns to the Compliance Manager must include:
  - (a) providing relevant advice and information to the Licensee for the purpose of ensuring its compliance with this Condition and with the Compliance Plan;
  - (b) monitoring the effectiveness of, and the Licensee's compliance with, the Compliance Plan;
  - (c) investigating any complaint or representation received by the Licensee from any person in respect of any matter arising under or by virtue of this condition or in relation to the Compliance Plan;
  - (d) recommending and advising upon the remedial action which any such **monitoring or** investigation has demonstrated to be necessary or desirable, including where necessary revising the Compliance Plan to reflect such recommendation and advice; and
  - (e) reporting regularly – at least annually, or with such greater frequency as the board of the Licensee may require or as may be specified in a notice issued by

the Authority to the Licensee from time to time – to the directors of the Licensee on:

- (i) his activities during the period covered by the report;
- (ii) the outcome of any investigations he has conducted during that period; and
- (iii) on his assessment of the Licensee's compliance with this Condition and with the Compliance Plan, clearly identifying any areas of non-compliance that he has identified and the remedial actions required in order to address them.

56. The Licensee must ensure that the Authority promptly receives a copy of each report that is given by the Compliance Manager to the directors of the Licensee.

#### **PART F – MODIFICATION OF RELEVANT DATE**

57. This Part F applies where an application has been made for an appeal to be brought under Article 14B of the Order against the decision by the Authority to modify the conditions of the Licence to include this Condition 42 (the **Modification Decision**), and the CMA has:

- (a) granted permission for the bringing of the appeal;
- (b) given a direction pursuant to paragraph 1 of Schedule 5A of the Order; and
- (c) confirmed the Modification Decision.

58. Where this Part F applies, this condition is modified such that each date specified in it by virtue of the Modification Decision is amended so as to be the date which falls seven months' later than was specified by virtue of that decision.

#### **PART FG. DEFINITIONS**

59. For the purposes of this condition:

**Associated Company**

means any company which is:

- (a) part of the EirGrid Group, but excluding the Licensee itself; and
- (b) (if not part of the EirGrid Group) an affiliate, ~~Related—Undertaking~~related undertaking or ultimate controller of the Licensee.

**Business Function**

means a set of activities carried on by the Licensee for the purposes of the Transmission System Operator Business which:

- (c) in the context of an application made by the Licensee for a Derogation, are as described by the Licensee in that application; and
- (d) in the context of any Derogation granted by the Authority following such an application, are as described by the Authority in that Derogation.

**Close Relation**

means, in relation to an individual, another individual who is their spouse (or partner of equivalent nature), parent, child, sibling, grandparent or grandchild.

**Compliance Manager**

has the meaning given to that expression in paragraph 53.

**Compliance Plan**

has the meaning given to that expression in

paragraph 46.

<b>Derogation</b>	has the meaning given to that expression in paragraph 23.
<b>Derogation Decision Date</b>	<p>means, in relation to any application for a Derogation made by the Licensee under Part C or Part D:</p> <p>(a) the date on which the Authority notifies the Licensee of its decision either to grant or reject <del>an</del>that application <del>for</del>; or</p> <p>(b) <del>where either paragraph 28 or 45 applies, the date on which a Derogation under Part C or Part D is deemed to have been granted.</del></p>
<b>Derogation Expiry Date</b>	has the meaning given to that expression in paragraph 31.
<b>Derogation Revocation Date</b>	has the meaning given to that expression in paragraph <del>33</del> 34.
<b>Effective Date</b>	has the meaning given to that expression in paragraph 20.
<b>EirGrid Group</b>	means EirGrid plc, each of its affiliates and Related Undertakings, and each company for which EirGrid plc or one of its affiliates or Related Undertakings is a holding company.
<b>European Electricity Transmission System</b>	means an entity which acts <del>(or at any time acted)</del> as electricity transmission system operator in any part of the United Kingdom, or any

<b>Operator</b>	member state of the European Union or the European Free Trade Area.
<b>European Energy Industry</b>	<p>comprises those entities engaged in carrying out the activities of:</p> <ul style="list-style-type: none"> <li>(c) the generation, transmission, distribution and supply of electricity; and</li> <li>(d) the storage, and the conveyance, shipping and supply through pipes, of natural gas,</li> </ul> <p>any part of the United Kingdom, or any member state of the European Union or the European Free Trade Area.</p>
<b>Executive Director</b>	means a director of the Licensee who is also an employee of the Licensee.
<b>Material Business Relationship</b>	<p>means any material business relationship between an individual and an entity, including in particular a relationship in which the individual acts as a provider of professional or consultancy services, or is involved in the supply of any other goods or services, to that entity, but shall not include (taken by itself):</p> <ul style="list-style-type: none"> <li>(c) the holding by an individual of a small number of shares or associated rights in the Licensee or any Associated Company; or</li> <li>(d) the receipt by an individual of any pension or other accrued benefit associated with</li> </ul>

prior employment or service with the Licensee or any Associated Company.

**Modification Decision** has the meaning given to that expression in paragraph 57.

**Non-Executive Director** means a director of the Licensee who is not an Executive Director.

**Principles and Guidance on Condition 42 Derogations** has the meaning given to that expression in paragraph 3536.

~~**Related Undertaking** in relation to a company, means any undertaking in which that company has a 'participating interest' with the meaning given to that expression in section 421A of the Financial Services and Markets Act 2000.~~

**Separate Management** has the meaning given to that expression in paragraph 21.

**Separate Resources** has the meaning given to that expression in paragraph 22.

**Services Agreement** means an agreement (whether or not legally-binding) between the Licensee and any Associated Company which relates to the provision or staff or other resources by the Licensee to that company, or by that company to the Licensee, or any sharing of staff or other resources between the Licensee and that company.

<b>Shared Management</b>	means managerial staff taking decisions in relation to activities carried out by the Licensee in the course of the Transmission System Operator Business which do not constitute Separate Management.
<b>Shared Resources</b>	means resources used in relation to activities carried out by the Licensee in the course of the Transmission System Operator Business which do not take the form of Separate Resources.
<b>Sufficiently-Independent Director</b>	has the meaning given to that expression in paragraph 17.



## Annex 2: Article 14(8) Licence Modification Notice

### Article 14(8) Notice

#### Decision published on modifications to the electricity transmission licence held by SONI Limited pursuant to Article 14(8) of the Electricity (Northern Ireland) Order 1992 (as amended)

In accordance with Article 14(2) of the Electricity (Northern Ireland) Order 1992 ("**the Order**") the Northern Ireland Authority for Utility Regulation ("**the Authority**") published on 24 January 2022 a notice ("**the Consultation Notice**") of its intention to modify the conditions of the electricity transmission licence ("**the Licence**") held by SONI Limited ("**the Licensee**").

The Consultation Notice indicated the proposal of the Authority to modify the conditions of the Licence by the incorporation into the Licence of a new Condition 42, the full proposed text of which was published together with that Consultation Notice.

In accordance with Article 14(5) of the Order the Authority has now considered the representations duly made to it following the publication of the Consultation Notice, and has decided to proceed with the making of modifications to the conditions of the Licence, in exercise of its powers under Article 14(1) of the Order, by incorporating within the Licence a new Condition 42.

In accordance with Article 14(8) of the Order the Authority hereby gives notice as follows –

1. The Authority has decided to proceed with the making of modifications to the conditions of the Licence held by the Licensee by the incorporation into that Licence of a new Condition 42.
2. On 24 January 2022 the Authority published a Consultation Notice stating that it intended to modify the Licence, providing a full text of the proposed new condition to be incorporated into it, and stating the reasons for and effect of the proposed modifications.
3. The purpose of that Consultation Notice was to bring the proposed modifications to the attention of the Licensee and other persons likely to be affected by them, and to invite representations or objections in connection thereto.
4. The Authority received nine responses to the Consultation Notice. The

Authority has taken into account the representations made therein, and made amendments to the proposed modifications where it considered it appropriate to do so for the fulfilment of its principal objective and statutory duties under Article 12 of the Energy (Northern Ireland) Order 2003.

5. The Authority has summarised the representations received in response to the Consultation Notice, stated how it has taken account of those representations, and described the changes it has now made to the modifications proposed in the Consultation in its paper entitled '*SONI TSO Governance: Decision on modifications to the SONI TSO licence*' ("**the Decision Paper**") published on 30 August 2022 together with this Article 14(8) notice.
6. The Decision Paper, at Chapter 4, states the reasons for and summarises the effect of the differences between the modifications which were subject to consultation by means of the Consultation Notice and the modifications which the Authority has (by virtue of this Article 14(8) notice) now determined to make to the conditions of the Licence.
7. The modifications now made, incorporating the changes made following the Consultation Notice, are shown in the new version of Condition 42 of the Licence and are set out (and shown in mark-up form, as against the provisions of Condition 42 published on 24 January 2022) in Annex 1 to the Decision Paper.
8. The reason why the Authority is making the modifications to the conditions of the Licence is to implement and give legal effect to its policy in respect of the governance of the Licensee in respect of the activities which are authorised by and/or the subject of obligations under the Licence. This policy, which is adopted in compliance with the Authority's principal objective and general duties under Article 12 of the Energy (Northern Ireland) Order 2003, is more fully described in Chapter 2 of the Decision Paper.
9. The Decision Paper, including its Annexes, shall be treated as an integral part of this Article 14(8) notice.
10. The Authority has, pursuant to Article 14(8)(a) of the Order, published this notice on its website and sent a copy of this notice to the Licensee. In addition, the Authority has provided a copy of this notice to the Department for the Economy and the Consumer Council for Northern Ireland.

The licence modifications taking the form of the incorporation in the Licence of a new Condition 42, the full text of which is reproduced at Annex 1 to the Decision Paper,

shall have effect on and from 26 October 2022.

Dated this day: 30 August 2022.

**Chief Executive**

**For and on behalf of the Northern Ireland Authority for Utility Regulation**

## Annex 3: SONI comments on Licence Modification text

Assessment of section 5 of the SONI response: Licence modifications

**NOTE:** The paragraph references, unless otherwise stated, are to those in the consultation version of the condition, but see Annex 1 for the updated version

Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
5.2	UR has failed to undertake a full reasons and effects assessment and that the proposed modifications fail in whole or in part to have their stated effect	We do not agree with this statement, the reasons and effects of the licence modifications were set out in section 7 of the consultation paper.	n/a
5.3	the licence modifications are, in many cases, insufficiently clear and precise and are likely incapable of being complied with.	We do not agree with this statement. In its comments SONI has not identified drafting where modifications are 'insufficiently clear and precise and are likely incapable of being complied with.'	n/a
5.3	In some cases, they directly contradict other conditions of SONI's TSO licence. In other cases, they demonstrate an inappropriate level of micro-management by the UR.	We do not agree with this statement. SONI's comments identifying contradictions are addressed in turn below.	n/a
5.3	Nor is it clear how the new Condition is "requisite or expedient" having regard to the UR's statutory duties under the 2003 and 2007 Orders, as Article 11(1) of the 1992 Order requires.	Condition 42 furthers UR's principal duty in Article 12(1) of the 2003 Order. The condition secures the interests of consumers of electricity now and in the long term through improved governance which improves transparency and accountability in how SONI delivers its TSO licence conditions. See section 2 of the decision paper.	n/a

Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
		Our duties under the 2007 SEM Order do not apply in this case as the matter is not a SEM matter.	
<b>5.4</b>	<b>Key concerns listed:</b>		
	Drafting potentially overrules SEMC decisions and network code obligations and allows the UR to add additional/different unspecified conditions.	The licence conditions provide for future decisions to be taken on derogations, and these may also be taken in individual cases by SEMC as a SEM matter where the SEMC has chosen to classify the decision as such.	n/a
	Contradictions/Conflicts with existing licence conditions and no assessment appears to have been completed as part of the reasons and effects section of the consultation. The UR has not proposed any modifications to the existing conditions to address these	SONI's comments identifying contradictions are addressed in turn below.	n/a
	The UR has delegated many of the proposed changes to guidance or future potential modifications. As such, SONI is unable to assess the effects of the modifications proposed. SONI would have expected the UR to have assessed the impact of its proposals against all licence conditions	We have not delegated 'proposed changes to guidance or future potential modifications.' The Principles and Guidance will be designed to assist SONI in making a derogation application. Future decisions will be taken as part of the derogation decision and these cannot be pre-empted now in advance of the evidence to support them becoming available.	n/a
	The Role of the Parent company and shareholder in relation to 'articles of association' and 'scheme of delegation'	See response to 5.27 and 5.28 below.	n/a
	Lack of published guidance documentation means that SONI cannot undertake a full assessment of the impact of the proposed modifications. This leaves SONI having to consider how the licence modifications will work as abstract concepts without any substantive guidance as	See response to 5.45. SONI's comments identifying contradictions are addressed in turn below.	n/a

Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
	to how they will operate in practice		
	Hard coded dates may penalise SONI if the UR delays its decision. Further, by binding itself to these dates, the UR risks undermining the consultation itself should they prove unworkable.	See response to 5.6, 5.46 and 5.47-5.48 below.	n/a
	There are no definitions for “Compliance Plan” and “Compliance Manager” despite them being highlighted in bold and it is unclear how this drafting aligns with Condition 12 of the SONI TSO Licence.	See response to 5.64-5.69	Yes
<b>5.6-5.11</b>	<b>PART A: The Principal obligation (Paragraph 2 of licence conditions)</b>		
5.6	hard coded dates in the proposed drafting limits the timeframe that may be required by the UR to review the responses to the consultation and address all concerns raised	The date by which the new SONI board should be in place will be pushed back from 1 January 2023 to 1 June 2023 reflecting the delay in the publication of UR’s decision on the licence modifications. For the same reason we have revised a number of other dates in the condition. See section 4 of the decision paper.	Yes
<b>5.12-5.15</b>	<b>The third requirement (Paragraph 5 of licence conditions)</b>		
5.12	The UR does not make any reference to experience of the regulated energy sector and system operations being limited to the European Energy Industry	This is incorrect as Paragraph 7.3f must be read alongside the licence modification text. See Part A, Paragraph 5 of the draft license conditions which explain the ‘third requirement’ and the related definition of European Energy Industry	n/a
5.13	What the UR is proposing will have the effect of a "closed shop" of directors who will likely know and have had regular dealings with each other. This can only	We do not agree with this claim. The need for specific energy experience is limited to one half of SIDs and no more. This is	n/a

Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
	promote group-think and not achieve the desired outcome	<p>appropriate as the TSO role is complex and specialised and the Board must have the knowledge and skills to hold the SONI management team to account.</p> <p>In addition the definitions of European Energy Industry and European Electricity Transmission System Operator are drafted to ensure that this is a very wide pool – both in terms of the activities where experience may be evidenced and the geographic pool of candidates.</p> <p>Candidates may have experience in generation, transmission, distribution and supply of electricity or in the storage, conveyance, shipping and supply through pipes, of natural gas.</p> <p>The geographic pool of candidates is very wide and covers the UK, all 27 EU countries (including Republic of Ireland) and the 4 countries of EFTA.</p> <p>UR has not limited the size of the board which should make it easier for SONI to ensure an appropriate balance of skills and experience on the board.</p>	
5.14	There is an inconsistency between the reasons and effects presented and the associated drafting. The drafting appears more restrictive (as European experience is specified). Therefore the effect of the drafting is not fully considered in the consultation paper.	We do not agree with this claim. See the response 5.13 which equally applies here.	n/a
5.15	Forecast costs in Table 5 do not account for any travel costs that may be incurred if board members are European based	Agreed but these costs, should they arise, are likely to be very small and would make no material difference. We have therefore not	n/a

Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
		altered the CBA to account for them	
<b>5.16</b>	<b>The fifth requirement (Paragraph 7 of licence conditions)</b>		
5.16	SONI notes that Paragraph 7 of the condition does not feature at all in the consultation paper. In order to ensure continuity it requires the terms of appointment of the SIDs to be staggered so that no more than one-third of those appointments are due to expire at the same time.	This requirement is self-explanatory.	n/a
<b>5.17-5.23</b>	<b>The twelfth requirement (Paragraph 14 of licence conditions)</b>		
5.17	It is unclear as to what action and when each action is expected to be taken in respect of reserved matters	Condition 42 will come into force once the licence modification comes into effect on 26 October 2022, but specific requirements of the condition with which SONI is being allowed time to comply clearly specify the date by which they are required to be complied with.	n/a
5.18-5.19	The role and rights of the parent company are not reflected in the drafting and new drafting is needed to state that subparagraphs (a) to (f) are subject to the rights of the Licensee's parent company	The present role of the parent company in SONI TSO matters would be altered by Condition 42 and in particular the drafting in subparagraphs (a) to (f). However, the parent company's role under the Companies Act 2006 is not affected (see the thirteenth requirement).	n/a
5.20	Suggestion that the UR is over reaching and the modifications put the board in conflict between its fiduciary duties to its shareholders and its licence	See response to 5.18-5.19.	n/a
5.21	Part (e), this contradicts Condition 3, Paragraph 13. These related conditions should be amended for consistency.	There is no contradiction as the twelfth requirement relates to matters reserved to the board.	n/a
5.22	In respect of Part (f), it is unclear how the Compliance Manager will interact with the requirements under	See response to 5.64-5.69.	n/a



Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
	Condition 12		
5.23	at Paragraph 7.3 j. (iii) there is a reference to Part B of the licence which should read Part C of the licence	The reference to B is correct as the licence conditions allow a derogation from Part B requirements. The application for derogation is made under Part C or D.	n/a
<b>5.24-5.25</b>	<b>The thirteenth requirement (Paragraph 15 of licence conditions)</b>		
5.24-5.25	The legal rights of the parent company and shareholder are not reflected in the drafting and the reference to the Companies Act 2006 is inadequate.	We do not believe that any parent company rights are being violated and no specific rights have been specified by SONI. The relationship between EirGrid and SONI is relatively unconstrained by the SONI TSO licence. The new licence condition will alter that but that is not the same thing as an infringement of parent company rights. EirGrid is the parent company of a highly regulated licensed business in NI and therefore should expect that the regulator may wish to make governance adjustments from time to time, including changes to the composition of the SONI board. This is not a new concept as the experience of other regulated businesses demonstrates, e.g. GB water companies and National Grid. The parent company's role under the Companies Act 2006 is not affected (see the thirteenth requirement).	
<b>5.26-5.28</b>	<b>The fourteenth requirement (Paragraph 16 of licence conditions)</b>		
5.26	The legal rights of the parent company and the shareholder are not reflected in the drafting	See response to 5.24-5.25.	
5.27 and 5.28	Only SONI's shareholder can amend the Articles of	The proposals can legally be implemented in	Yes

Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
	Association and any amendment would not be valid without the consent of the Minister. As a result SONI cannot meet the requirement to amend the Articles of Association without causing both itself and EirGrid to breach the EirGrid Act. Therefore the proposals cannot legally be implemented in accordance with Irish law.	accordance with Irish law once the consent of the Minister is obtained. It is EirGrid's responsibility as ultimate controller to obtain this on behalf of SONI. See changes made to the licence modifications post consultation and explained at Paragraphs 4.15-4.16 of the decision paper. These ensure that the requirement on SONI to ensure the modification of its Articles of Association are an absolute obligation rather than being subject to best endeavours.	
<b>5.29-5.30</b>	<b>PART B: The Principal Obligation (Paragraph 18 of licence obligations)</b>		
5.29	The drafting of the Principal Obligation appears to contradict Condition 3(13) and the interaction of these two licence conditions was not highlighted or discussed in the consultation.	There is no inconsistency. The prohibition in Condition 3(13) is applicable only in the three defined circumstances set out in that provision. UR is not aware that any of those circumstances applies at the present time, but if it did SONI may apply to UR for the consent referred to in the provision if it were needed for the purposes of complying with any other obligation under the licence. The principal obligation under Condition 42 is a separate and additional requirement that must be complied with in any event.	
5.30	This is a fundamental change in paradigm from "permitted unless" to "prohibited unless"		
<b>5.31-5.32</b>	<b>The Exception (Paragraph 19 of licence obligations)</b>		
5.31	It is unclear how Condition 42(19) fits into the legal hierarchy, e.g code obligations which have already been approved and which have been implemented on an integrated basis with EirGrid. SONI may need to seek a derogation in order to meet a legal requirement and also	Paragraph 7.6 of the consultation paper is explicit that except in respect of those functions for which a derogation has been granted the SONI TSO business will from 1 July 2024 need to be managerially and operationally separate	n/a

Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
	remain licence compliant.	from EirGrid and any other company within the EirGrid Group. Therefore if SONI is to continue with arrangements that are integrated with EirGrid a derogation will be needed. SONI understands that this is the effect of Condition 42 as the sentence at the end of its Paragraph 5.31 makes clear <i>'SONI may need to seek a derogation in order to meet a legal requirement and also remain licence compliant.'</i> The consultation also makes clear that the evidential burden when seeking a derogation lies with SONI.	
5.32	This risk was not highlighted or discussed in the reasons and effects presented by UR.		
5.33	Key Definitions (Paragraph 20 of licence obligations – definition of the 'Effective Date')		
5.33	SONI considers that the UR's proposals will require full implementation of a new price control. Therefore the timelines presented are unlikely to be achievable.	The additional costs detailed in the CBA, e.g. those required to establish and maintain a new SONI Board, can be facilitated under the existing price control via uncertainty mechanisms. See section 5 of the decision paper. We expect SONI to consider whether to apply for a derogation based on what is most efficient for its business and this could be continued integration with EirGrid in many cases. Where this is the case and a derogation is granted, we would not expect existing allowances would need to change.	n/a
5.34-5.37	Paragraph 21 of licence obligations		
5.34 and 5.35	Whether point (c) of the definition should apply to an 'ultimate controller' of the Licensee as this appears to	We do not agree that this would be the case. The definition restricts the type of relationship	n/a

Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
	<p>preclude actions such as paying a dividend.</p> <p>It has also been drafted so widely that it will prohibit many of the existing contractual arrangements between SONI and its parent company.</p>	<p>which SONI employees in a management role may have with any associated company. This would not affect the payment of any dividend That is correct. SONI may apply for a derogation if it wishes to.</p>	
5.36-5.37	<p>The term Associated Business is already defined in the SONI licence, and has a similar, but different definition to 'Associated Company' the new drafting will introduce potential confusion and conflict between terms</p> <p>The UR should consider excluding a relevant holding company from the term Associated Company, consistent with its exclusion from the term Associated Business under Condition 12</p>	<p>The definition of 'associated company' and in particular the treatment of the holding company is necessary to ensure separation of the SONI TSO business from EirGrid and any other company within the EirGrid Group.</p>	n/a
5.38-5.41	Paragraph 22 of licence obligations		
5.38- 5.39	<p>It is unclear whether the requirement (that managerial and operational resources are not shared or accessible to any Associated Company) contradicts the requirements of Licence Condition 3 where SONI is required to have at all times sufficient resources to comply with its obligations as TSO</p> <p>SONI has numerous licence conditions as well as other obligations (e.g. Network Codes) where it needs to have the ability to share systems or data with the Republic of Ireland System Operator</p>	<p>There is no contradiction. Where SONI wishes to avail of EirGrid resources, it will need a derogation granted by the UR</p>	n/a
5.40	<p>Under part (c), SONI will be limited in what data it can share. However, it is unclear how this drafting interacts with the requirements under Condition 11 and in particularly Paragraphs 4(c) and 4(d).</p>	<p>We have made a drafting change to Condition 42 Paragraph 22(c) to make it clearer that where a derogation is not in place, any data sharing between SONI and EirGrid (and/or any other Associated Company) shall be in accordance with the terms of the SOA and that</p>	Yes

Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
		those terms shall reflect the requirements of Condition 11(4)(d). See Paragraphs 4.20-4.21 of the decision paper for further explanation.	
5.41	UR has failed to undertake an appropriate reasons and effects assessment therefore the drafting is an error as the proposed modifications fail to achieve, in whole or in part, the effect stated by the Authority	We do not agree this is the case.	n/a
5.42	Paragraph 24 of licence obligations UR should use relative dates rather than hard coded dates as the time period for its consultation is unknown at this stage	See response concerning Paragraph 5.6 above.	Yes
5.43-5.45	Paragraph 25 of licence obligations (application for derogation)		n/a
5.43-5.44	Paragraph 25(d) contradicts the UR's intention as asset out in Paragraph 6.22 of the consultation	There is no contradiction. 6.22 reflects on the responsibility of the SONI Board. Condition 42 Paragraph 25(d) seeks to ensure that an application for derogation covers the matters referred to in 25(d).	n/a
5.45	The Guidance referenced in 25(e) has not been consulted on and this puts SONI and other stakeholders at a disadvantage	A draft of the guidance will be published for consultation after this decision on the licence modifications. It will be designed to assist SONI in making a derogation application but the fact that it is not yet published does not hinder SONI in considering, or taking steps to comply with the initial obligations under, Condition 42.	n/a
<b>5.46</b>	<b>Paragraph 26 of licence obligations</b>		
5.46	UR should include a 'minded-to' stage in the derogation process similar to the TNPP process	We are happy to consider the need for this on a case by case basis, but as with the TNPP process it is not necessary to hard code it into the licence.	n/a
<b>5.47-5.48</b>	<b>Paragraph 27 of licence obligations</b>		

Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
5.47-5.48	<p>UR should use relative dates rather than hard coded dates as the time period for its consultation is unknown at this stage</p> <p>UR has failed to consider the impact that these changes may have on existing or planned workstreams over the period 2022 to 2024 – e.g. future system services programme or other SEMC related work. It is unclear at this stage whether the implementation will be such that SONI will be able to or need to seek a derogation</p>	<p>See response concerning Paragraph 5.6 above</p> <p>SONI should factor existing and planned work streams (including SEMC related work streams) into its assessment when considering what derogations it wishes to apply for.</p> <p>After September 2023 if an unforeseen issue arises under Paragraph 41 UR could bring forward the date on which the application could be made. We have made a drafting change to clarify how UR will exercise the power to vary time periods (Condition 42, Paragraph 42). See Paragraph 4.37 of the decision paper</p>	Yes
<b>5.49</b>	<b>Paragraph 29 of licence obligations</b>		
5.49	<p>Unclear why the drafting under (29)(b) has been included. There is no discussion of it under the reasons and effects section and it may cause confusion or conflict with the existing licence obligations (Condition 7).</p>	<p>This drafting affirms SONI's obligations in this context and does not conflict with Condition 7.</p>	n/a
	<b>Paragraph 30 of licence obligations</b>		
5.50-5.51	<p>The drafting in 30 (b) (ii) would allow the UR to change any aspect of a derogation request and put this obligation on SONI without any method to appeal</p> <p>The UR has not provided any narrative on the effects of this condition in its consultation. This wording should be removed from the drafting.</p>	<p>30 (b)(ii) provides flexibility which the UR needs in circumstances in which it cannot accept the entirety of the proposed definition of a Business Function advanced by SONI as part of its application. It could be used, for example, where the information provided in support of the application justifies the granting of a derogation in respect of some of activities within the Business Function as defined in the application but not all. This flexibility is to the benefit of</p>	n/a

Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
		SONI. It allows for decisions which are tailored to the circumstances of the case. The alternative, which is that an application had to be rejected if the definition of the Business Function in respect of which it was made was considered incorrect, would not be likely to assist SONI or be conducive to achieving the best and most proportionate outcome.	
<b>5.52-5.53</b>	<b>Paragraph 31 and 32 of licence obligations</b>		
5.52-5.53	SONI is concerned that UR may place additional obligations on SONI by attaching conditions to the approval of derogation and that SONI has no right of appeal. The UR has not provided any narrative on the effects of this condition in its consultation. This wording should be removed from the drafting.	We cannot prescribe potential conditions in advance since by definition they need to be adjusted to be responsive to the particular circumstances of the case. SONI will have a right of challenge via judicial review.	n/a
<b>5.54-5.56</b>	<b>Paragraph 33 of licence obligations</b>		
5.54-5.56	There is an inconsistency between the 6 month period to implement any revocation of a derogation and the 12 month period for implementation of a derogation. The 6 month period is not discussed in the consultation.	The shorter period reflects the fact that revocation is taking place by virtue of material non-compliance. In these circumstances (which are entirely avoidable, within the control of SONI) it may be inappropriate for SONI to continue to benefit from the derogation for a lengthy period given that it has failed to comply with the conditions to which it was subject. However, UR has a discretion which allows it to respond appropriately to the circumstances of the case. If justified, the period of time may be longer than six months as provided for in	n/a

Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
		Paragraph 33(b), which states only that six months is a minimum	
<b>5.57-5.59</b>	<b>Paragraph 35 of licence obligations (the Principles and Guidance)</b>		
5.57-5.59	The Principles and Guidance has not been consulted on by the UR and the draft states that the UR 'may issue' this. SONI considers that this should be updated to 'will issue.'	The guidance will be consulted on following the decision to modify the licence. Therefore no change to the licence drafting is needed.	n/a
<b>5.60-5.63</b>	<b>Paragraph 36 of licence obligations</b>		
5.60-5.63	SONI is unclear of the logic of the approach of waiting 4 years before having the ability to seek further derogations. EU related requirements and network codes as mandated by the Withdrawal Agreement are expected to evolve as are the future system service arrangements. Whilst the UR has included a provision for earlier directions to be issued (Paragraph 40), it is unclear what process this will follow and what lead times will be allowed.	The period is intended to provide some stability in arrangements but equally the provision allowing UR to bring forward any date in Part D (Paragraph 41 in the consultation text – now Paragraph 42) is a recognition that things may change over time (including SEMC work programmes). We consider Paragraph 41-42 to be sufficiently flexible for this purpose, taken together with the addition of a new Paragraph 43 which makes clear that it can be used in a targeted way to adjust timescales for particular purposes.	n/a
<b>5.64-5.73</b>	<b>PART E: The Compliance Plan</b>		
5.64-5.69	SONI considers that there is a significant conflict between these conditions and Condition 12. The UR has clearly omitted a “consequential change” to extant licence conditions therefore the proposals are incomplete. The drafting replicates existing provisions in condition 12, including definitions which is confusing.	There is no conflict. The licence conditions set out in Part E are for the purpose of monitoring and facilitating compliance with the requirements of Condition 42. Condition 12 requirements have a different purpose and therefore the two sets of requirements are distinct and each standalone. We acknowledge that Condition 12 could benefit from some	n/a



Reference (Paragraph no. from response)	Concern raised	UR response	Suggested alternative drafting (if necessary)
		amendment for clarity, but that does not impact on Condition 42. For clarity we have included two new definitions – ‘Compliance Manager’ and ‘Compliance Plan’	
5.70-5.73	UR has stipulated that a compliance plan must be delivered to the UR by no later than 1 January 2023. A longer transition period is needed to ensure appointment of the compliance manager, completion of a compliance assessment and input by the new SONI board.	We have adjusted the date by which SONI is required to submit the first compliance plan under Condition 42 from 1 January 2023 to 1 December 2023	Yes
5.74	Paragraph 55 of licence obligations – definition of ‘Associated Company’ (if not part of the EirGrid Group) – It is unclear if this mean “if SONI is not part of the EirGrid Group”, or if the other company is not part of the Group	It means the latter	n/a

## Annex 4: EirGrid comments Licence Modification text

### Assessment of the EirGrid response: Licence modifications

**NOTE:** The Paragraph references, unless otherwise stated, are to those in the consultation version of the condition, but see Annex 1 for the updated version

Reference (Paragraph no. from response)	Theme	Concern raised	UR response	Suggested alternative drafting (if necessary)
<b>40-62</b>	<b>EirGrid response to the UR's proposed licence modifications</b>			
40-41	Inconsistency with existing licence conditions	Condition 42 is inconsistent with SONI and EirGrid's TSO licences as both TSOs are required to 'act in conjunction' with each other. The new modification would introduce a separation between SONI and EirGrid and EirGrid does not understand, nor has UR explained, how they can be expected simultaneously to operate entirely separately yet also be expected to work 'in conjunction with' each other.	There is no inconsistency. The SEM requires acting in conjunction, collaboration and cooperation between the two TSOs but not integration of TSOs or the creation of a single TSO. The governance arrangements undermine SONI's ability to comply with its 'acting in conjunction' licence obligations and could expose SONI to potential enforcement action for breach of its TSO licence. See annex 6 of the decision paper.	n/a
42-50	Inconsistency in treatment compared to other licence holders	Approach taken by UR goes much further than that taken by UR in respect of other regulated licence holders, notably NIE Networks. <ul style="list-style-type: none"> <li>18<sup>th</sup> requirement and UR role in SONI Board appointments;</li> </ul>	UR has a similar role in NIE Board appointment to that proposed for SONI. See Condition 3A (1)(b) of the NIE Networks Participate in Transmission licence. <ul style="list-style-type: none"> <li>The new SONI licence condition does not enable UR to approve the</li> </ul>	n/a

		<ul style="list-style-type: none"> <li>• Restriction of EirGrid's legitimate right as shareholder in exercising corporate governance and control over its subsidiary; and</li> <li>• More stringent separation and independence required between EirGrid and SONI as opposed to between ESB and NIEN</li> </ul>	<p>appointment of SONI Directors that rests with SONI. However, and as explained in the January 2022 consultation paper (see Paragraph 7.4(f)), before an appointment is made UR can exercise a right of veto if it considers that the relevant criteria for the appointment of sufficiently independent directors are not met in any individual case. This process step is intended to provide SONI with some assurance that UR will not consider Board appointments as in breach of the relevant requirements after the appointment is made and when it would be much more difficult to unwind.</p> <ul style="list-style-type: none"> <li>• We acknowledge that ESB retains ultimate responsibility for appointments to the NIE Networks board whereas this will not be the case for EirGrid and appointments to the SONI Board. However, changes in EirGrid's current largely unconstrained relationship with SONI (and in particular an independent board) are necessary in order to ensure an independent SONI TSO in circumstances where there is much scope for EirGrid to perform SONI's TSO functions, and where SONI must be able to act in conjunction for SEM</li> </ul>	
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			<p>purposes. NIE Networks' relationship with ESB is currently characterised by separation not integration and ESB and NIE Networks have no need to act in conjunction for SEM purposes. Therefore more stringent governance structures can apply to SONI compared to NIE Networks.</p>	
51	Impingement on EirGrid's rights as owner and shareholder	EirGrid may appoint only one member to the SONI board	This is necessary in order to ensure an independent SONI TSO	n/a
52-57	Contravene the current legal framework in place for EirGrid and unworkable	<p>SONI's Articles of Association would require change and this requires Ministerial consent in Republic of Ireland. Under the Irish Code of Practice for the Governance of State Bodies EirGrid must exercise appropriate oversight and control of its subsidiaries, including SONI. Therefore the modifications are not capable of being affected by either the Board of SONI or the Minister. The Government of Republic of Ireland cannot overlook its own codes of practice. The level of prescription is unusual and may not constitute a lawful modification. The modifications are unworkable.</p>	<p>The proposals can legally be implemented in accordance with Irish law once the consent of the Minister is obtained. See in particular sections 5(2) and 5(3) of Electricity Regulation (Amendment) (EirGrid) Act 2008<sup>84</sup> which state:</p> <p><i>5.— (1) EirGrid may not, without the approval of the Minister given with the consent of the Minister for Finance, acquire, establish or dispose of subsidiaries or invest in other undertakings.</i></p> <p><i>(2) Without prejudice to EirGrid exercising any of its functions, a subsidiary of EirGrid may exercise such and so many of EirGrid's functions as are provided for in the memorandum and articles of</i></p>	n/a

<sup>84</sup> [Electricity Regulation \(Amendment\) \(Eirgrid\) Act 2008, Section 5 \(irishstatutebook.ie\)](http://irishstatutebook.ie)

			<p><i>association of the subsidiary.</i></p> <p><i>(3) An alteration in the memorandum of association or articles of association of a subsidiary of EirGrid shall not be valid or effectual unless it is made with the consent of the Minister.</i></p> <p>It is EirGrid's responsibility as ultimate controller to obtain the Minister's consent on behalf of SONI and EirGrid has given no reason why it is likely that this consent would be withheld.</p> <p>In regard to the Republic of Ireland Code of Practice for the Governance of State Bodies<sup>85</sup> we note that, as a subsidiary of EirGrid which is established in the UK, SONI is subject to the UK legal framework including the licence under which SONI operates. But, the UK framework is not subject to the Republic of Ireland Code of Practice.</p> <p>It is for EirGrid to reconcile the requirements of the code with UK rules applicable to SONI. We note that where needed the Code (see the section entitled 'Compliance Requirements') provides flexibility for companies to suitably adapt the code where they consider that certain aspects of it may have a disproportionate effect on them (e.g. because of the nature and scale of their activities), provided this is agreed and documented with the</p>	
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<sup>85</sup> - [1d213280-29b8-41ec-92c4-ca8974db5224.pdf \(www.gov.ie\)](#)

			relevant Minister/parent Department.	
58-62	UR bias against EirGrid	<p>Proposals portray a prejudice against EirGrid when compared to:</p> <ul style="list-style-type: none"> <li>• Regulation of NIEN;</li> <li>• Differing treatment of MEL during the governance review conducted of MEL, both in terms of engagement and the outcome of that review</li> </ul>	<p>See above in response to 42-50</p> <p>We disagree with EirGrid's views on bias with reference to the MEL governance review. That review was in fact the second review of corporate governance of MEL and concerned the MEL gas transmission companies. MEL is a mutual company, unique in the NI energy industry and therefore very different to the EirGrid Group. MEL's response to the January licence modification consultation noted that MEL's governance arrangements are not analogous to that of SONI within the EirGrid Group. We agree - the outcomes of the two reviews cannot be compared.</p> <p>We also reject the allegation that we have failed to engage meaningfully with EirGrid on SONI governance. See Paragraph 3.18 of the decision paper.</p>	n/a
<b>63-80</b>	<b>The UR's proposed derogation process</b>			
63-66	Increased cost	<p>An arm's length contractual SLA type approach would fundamentally alter the Group cost allocation and recharge policy. Commercial terms attribution with appropriate margins and benchmarked counterfactuals would give rise to significantly greater costs to the SONI business and NI consumers</p>	<p>An SLA would be a fundamentally different and transparent approach compared to the current Cost Allocation and Recharge policy. We envisage the SLA as a contractual arrangement between EirGrid and SONI which will:</p> <ol style="list-style-type: none"> <li>1. Be signed off by the SONI Board;</li> <li>2. Include service specifications and rates; and</li> <li>3. Be legally binding between SONI and EirGrid plc.</li> </ol>	n/a

			<p>This will ensure transparency and scrutiny by SONI over the costs it pays EirGrid for services and also the costs EirGrid may pay SONI for use of SONI staff/resources. SONI may wish to benchmark the costs for services paid under the SLA with market rates elsewhere to assess and ensure value for money.</p> <p>EirGrid's view is that an SLA is likely to give rise to significantly greater costs than the current arrangements as it would be based on an 'arm's length' arrangement on the basis of commercial terms rather than costs attribution. In other words SONI and EirGrid would treat each other as unrelated companies each seeking commercial advantage.</p> <p>We do not agree that EirGrid and SONI have any commercial incentive to behave in this way as it would likely result in increased costs for all consumers for common services, the underlying costs of which would not change. UR would not agree to inefficient costs (including a margin) in circumstances where costs could otherwise be allocated fairly by means of an agreed cost attribution approach governed by an SLA.</p> <p>If the implementation of an SLA results in any hidden cross subsidies between the two jurisdictions being revealed as better information becomes available, then</p>	
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			eliminating these cross subsidies will be a positive outcome of the governance review.	
67-75	Extent of derogation and SOA impact	<p>Despite the derogation process there is no situation where the current arrangements could be expected to continue</p> <p>To fulfil its licence obligations the scope and number of derogation would be expected to be significant</p>	<p>We do not agree with this view. The derogation process is designed to exempt SONI from the general requirement to be managerially and operationally independent from EirGrid, provided that a case can be made by SONI for an exemption. Any current arrangement which is the subject of a successful application for a derogation from the independence requirements may continue.</p> <p>The scope and number of derogations to apply for is a matter for the SONI Board, there is no limit on the number that may be applied for</p>	n/a
76-77	The derogation process creates four hurdles to achieve economic synergies where none exist at present	<ol style="list-style-type: none"> <li>1. The need for derogation may not be identified in time by SONI;</li> <li>2. SONI Board Approval - The test required by the SONI Board to determine if the derogation is ultimately to the benefit to NI customers. If this cannot be provided, the SONI Board cannot apply for derogation;</li> <li>3. UR may not grant the derogation;</li> <li>4. It may not be rational for EirGrid to agree to the proposed derogation</li> </ol>	<p>The derogation process is designed to ensure transparency and evidence based outcomes, the issues identified by EirGrid fall to be managed by SONI.</p> <ol style="list-style-type: none"> <li>1. When considering what derogations to apply for SONI should take into account all existing and planned work streams. The timing of the subsequent derogation process may also be varied – see UR response to Paragraphs 5.47-5.48 of SONI response</li> <li>2. The requirements as to content of an application is set out in</li> </ol>	n/a



			<p>Paragraph 25 of Condition 42. An application must meet these requirements and the SONI board should assess this before an application is submitted. The question of whether an application will result in a derogation being granted is a separate consideration and falls to UR or the SEMC as the case may be.</p> <p>3. The derogation process puts the evidential burden on SONI who is best placed to bear it. The January 2022 consultation noted that SONI has already put forward information to substantiate its view that the existing arrangements for single system operations have delivered benefits to consumers. This information illustrates that SONI should be capable of providing a robust case with clear justification for a derogation in this area. If the case for integration with EirGrid is as strong as SONI asserts it to be then an independent SONI board should have little difficulty in discharging that evidential burden.</p> <p>4. We note that Condition 3(11) of SONI's licence requires EirGrid to refrain from any action which would be likely to cause SONI to</p>	
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			breach any of its obligations in the licence.	
78	Potential for EirGrid breach of licence	EirGrid could be in breach of its TSO Licence solely on the basis of action, or inaction by SONI or by an absence of the UR taking the appropriate decisions, e.g. acting on conjunction obligations	The Condition 42 derogation process contains clear timescales for SONI and UR. Also where an application for derogation has not been granted by UR by the necessary date it shall be deemed granted in accordance with the provisions of Condition 42(28) Integration of SONI into Eirgrid plc is not a prerequisite for the two TSOs to collaborate and act in conjunction	n/a
79-80	Inconsistency with existing licence conditions	<p>Condition 3 of the EirGrid TSO licence will require amendment (by SEMC) in regard to the exercise of EirGrid functions in the interests of consumers in both Republic of Ireland and NI</p> <p>The proposed Condition 42 would have to include a specific exclusion of applicability in the context of Condition 1, 3, 7, 11, 12, 22, 22A, 22B, 23, 23A, 23B, 29, 33, 35, 39 of SONI's TSO Licence at which point it would effectively become meaningless.</p>	<p>We do not agree with this assertion – for the reasons set out in the January 2022 consultation our governance proposals do not disturb this EirGrid licence condition (see from 5.4-5.6 of the January 2022 paper).</p> <p>The licence conditions cited regulate EirGrid/SONI interactions or otherwise require SONI to act in conjunction with, in cooperation with, or in consultation with EirGrid TSO.</p> <p>For the reasons explained in response to Paragraphs 40-41 above, there is no inconsistency between Condition 42 and requirements on SONI to act in conjunction or otherwise collaborate with EirGrid TSO.</p> <p>The derogation process itself will determine whether certain Business Functions should be exempt from the</p>	n/a

			<p>general requirement to be managerially and operationally independent from EirGrid. The information to inform these decisions will be provided by SONI as part of the derogation process. These decisions cannot be pre-determined now in the absence of evidence to support them.</p>	
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# Annex 5: Potential for policy divergence increasing risk of harm for NI consumers

## Introduction

This Annex sets out a number of examples of areas where policy divergence between NI and Republic of Ireland may occur and if not managed appropriately by SONI TSO, could act to cause harm to consumers. It should be noted that this is a set of illustrative examples:

The examples are organised into three areas as follows:

- Generation Mix:
  - Small scale wind generation
  - Nuclear;
- Smart Metering; and
- Offshore Cables and Networks

We also consider the policy work underway in GB to ensure greater independence of the electricity system operation through the 'Future System Operator' (FSO) project. The extent to which NI government policy may wish to see something similar for NI is not clear at this stage.

## Generation Mix

It is possible that the types of generation connected to the systems of NI and Republic of Ireland will differ. These differences in turn could deliver different benefits and challenges in operating and developing the associated power system and networks.

We set out two examples of potential differences in generation mix below, each of which did, or would, flow from policy differences between NI and the Republic of Ireland. These relate to:

- The deployment of small-scale wind turbines; and
- The potential future deployment of nuclear generation

## Small Scale Wind Generation

To date, most renewable generators have benefited from explicit support mechanisms, and would not have been built in the absence of those mechanisms. These mechanisms (for example) can serve to:

- Provide an additional payment to renewable generators. This is a feature of the early "Renewable Obligation Certificate" (ROC) scheme that operated in GB and NI. Generators were awarded a set number of ROCs for each MWh they generated, and could then sell these to licenced Suppliers<sup>86</sup>. The overall

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<sup>86</sup> Retailers of electricity

ROC scheme ensured that Suppliers were incentivised to buy ROCs to demonstrate the proportion of energy they had bought from renewable sources.

- Provide price certainty to renewable generators – guaranteeing the price they will earn for any output. This is a feature of the current renewable support mechanism operating in GB, and of the historic “ReFiT” support mechanism in the Republic of Ireland.

The detailed design of these support mechanisms will impact the relative economics of different renewable projects, with variations occurring, for example, by the scale or technology of the project. For the ROC scheme, this variation was most apparent in rules for how many “ROCs” a power station would get for each MWh of electricity it generated.

The rules adopted in NI for the allocation of ROCs led to the deployment of a large number of small-scale wind farms (there are 1305 wind generating renewables obligation accredited stations in NI). This, in turn, led to challenges for the electricity network in accommodating the electricity flows from those wind farms.

This legitimate policy difference between NI and the Republic of Ireland is one that should be accounted for by NI network companies. In this case, the NI network companies should proactively identify the policy and its impact, and then account for that impact in their plans to reinforce<sup>87</sup> their networks. This behaviour was not observed, with UR having to initiate work (on G-TUoS) with both SONI and NIE Networks to encourage them to address the issues.

## Nuclear

At present, there are no Nuclear power stations on the island of Ireland; however, this could change such that one or both of NI and Republic of Ireland allow such power stations to be built in its territory. Whilst this case is hypothetical it seems NI would be more likely than the Republic of Ireland to allow the building of Nuclear Power stations at some future point:

- One reason Nuclear power has yet to be deployed in Republic of Ireland is that traditional nuclear power stations are large relative to the electricity demand within the Irish system. For example, the European Pressurised Water Reactors come in units of ~1.5GW. This is large compared to demand across the island of Ireland<sup>88</sup> – making it expensive to accommodate such a large unit in a way that maintains reliable electricity supplies if the nuclear power station fails.

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<sup>87</sup> “reinforcement” is the general term for increasing the capacity to transport electricity in specific areas of a network.

<sup>88</sup> Forecast demand for electricity across Republic of Ireland and NI between March and June 2022 has the following characteristics: a minimum of ~2.9GW; an average of ~4.3GW; a maximum of ~5.9GW. Data sourced from SEMO. <https://www.semo.com/market-data/dynamic-reports/index.xml#BM-010>

- Whilst NI energy policy is separate to that for the rest of the UK, UK Government has recently affirmed the role of Nuclear power in the future electricity industry – including an intent to support the development of small scale modular reactors<sup>89</sup>.
- Small-Scale Modular reactors are typically considered to be up to 300MW, albeit the Rolls Royce example is larger – at 470MW. The capacity of these smaller scale generators is similar to that of other thermal generators on the Irish and Northern Irish power system, so could be accommodated.
- The Republic of Ireland has a long-standing anti-nuclear policy – which may make it less likely than NI to adopt nuclear power generation; however, this policy has been subject to some recent debate<sup>90</sup>.

Nuclear Power stations would offer some advantages to SONI and Eirgrid in addressing the challenges they would otherwise face in moving to low-carbon electricity system. These power stations provide services on which the current system relies, but which are not typically provided by other low-carbon forms of electricity generation. The key such service is inertia.

Nuclear power stations are likely to produce electricity through generating units that are relatively heavy, and which spin directly synchronised with the alternating current of the power grid. As relatively heavy units, these have energy stored in their motion, known as “inertia”. This energy is stored as the unit spins faster, and released (in the form of additional electricity generation) as the unit slows down.

Inertia has a value in helping keep electricity systems stable. In simple terms, as demand for electricity goes up, all directly synchronised generators will slow down – reducing the rate at which alternating current cycles (system frequency). As they slow down, these generators release some of their stored energy in motion (inertia), helping address the increase in demand, and slow the rate at which system frequency changes. In the absence of inertia, system frequency could become very unstable – making the power system difficult to manage, and causing issues for all users of electricity.

Wind and Solar generation tends not to be able to offer inertia for a number of reasons. How this is managed is an emerging energy policy issue being considered in many parts of the world; however:

- In each case, it is recognised that the Transmission System Operators have a unique insight into this area, as it is System Operation that is impacted; and
- The situation is more extreme for the island of Ireland, as most other AC systems will retain some inertia in the form of existing nuclear generation, and

<sup>89</sup>[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/1069969/british-energy-security-strategy-web-accessible.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1069969/british-energy-security-strategy-web-accessible.pdf)

<sup>90</sup><https://www.irishtimes.com/opinion/no-time-for-wand-waving-or-wishful-thinking-on-our-energy-supply-1.4887125>

the AC system is small compared to the Continental European AC system or that of GB.

To account for this, Republic of Ireland and NI are considering the direct purchase of inertia as a service<sup>91</sup>, with the TSOs (EirGrid and SONI) being responsible for identifying the quantity and location of inertia requirements, and for procuring that inertia. This is a key role, where NI industry and policy makers rely on the integrity and objectivity of SONI.

Were only one of NI or Republic of Ireland to sanction the building of Nuclear Power Stations, this would impact the requirements for procuring inertia from other sources, and lead to a risk of distorted competition in the provision of that service. This will depend on the nature of the competition, and on the detail of the contracts awarded – both areas where policy makers will seek advice from SONI. For example:

- The TSO's could judge that the system with nuclear generators has less need for inertia to be competitively procured, but should be provided "for free" by those nuclear generators – a potential distortion to competition;
- The TSO's could, inappropriately, judge that that system with nuclear generators needed less inertia than provided by those generators, so only pay them for a proportion of their inertia. Again, this could potentially distort competition; and
- The detailed contract terms for inertia provision could be more favourable to non-nuclear providers of inertia. Again, this could potentially distort competition.

## Smart Metering

"Smart Metering" describes a range of meters being deployed to small scale (e.g. residential) consumers in various parts of the world. The functionality of these meters varies. At a minimum, these meters will record MWh consumption of electricity on a time period (e.g. ¼ hour) basis and allow that consumption data to be read to a central database via a data communications network. Beyond this minimum, the range of capabilities offered by meters can vary significantly, with areas of variation including:

- **Quantities measured:** Whilst all meters will measure the consumption of active energy (MWh), some will also record details of reactive power usage (MVar);
- **Direction of flow:** Whilst all meters will record energy that is imported to a property to be consumed, some will also record energy that is exported. Such export could happen, for example, in instances when the solar panels on the roof of a house produce more energy than is consumed in that house;

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<sup>91</sup> <https://www.eirgridgroup.com/site-files/library/EirGrid/EirGrid-SONI-Plan-for-procurement-of-LCIS-Webinar.pdf>

- **Data pass through:** Some smart meters have the ability to use their existing communications to act as a gateway to other devices in the relevant user's property. For example, this could allow data to passthrough and switch certain devices on or off in a home, whilst keeping a record of that communication;
- **Full or Partial disconnection:** Some smart meters have the capability to disconnect the user on receiving the correct data over the communications network. This capability may then be full (no electricity can flow) or partial (meter "trips" if electricity flow goes above a threshold);
- **Poll Energisation status:** Some meters allow for remote access to detect whether there is energy getting to the meter. This facility is then used to diagnose faults in electricity networks, and to confirm that such faults have been resolved; and
- **Who has access:** Some smart metering systems are set up such that only one party can send and receive data from a meter, with others being more permissive.

These differences tend to be in the gift of policy-makers rather than the electricity user for a number of reasons:

- The roll-out of smart meters tends to be policy driven rather than consumer led, reflecting:
  - Economies of scale in this approach; and
  - That consumers typically perceive the value to them of a smart meter as less than the costs of providing and servicing that meter.
- Standards need to be applied to meter designs to ensure they are sufficiently accurate, and that they can be accessed by central systems that account for electricity usage.

These policy differences make it likely that the capability of smart meters in NI will differ from those in the Republic of Ireland. In this context, Republic of Ireland has already mandated the roll-out of relatively basic smart meters, whilst a rollout of smart meters has not been mandated for NI. In contrast GB has rolled out more capable meters. Any future policy for NI would consider both the GB and Republic of Ireland models. As NI smart metering policy evolves, it is possible that it will seek more capable meters than those deployed in the Republic of Ireland.

The capability of smart meters will impact measures to address domestic participation in electricity markets, and the extent to which such consumers can contribute in addressing the challenges in operating a low-carbon electricity system. For example:

- Measures to account for export from domestic electricity generation; and



- Measures to assess the performance of demand side response – this may be evidenced by a signal passing through a meter to activate demand response

## Offshore Transmission Cables and Networks

There are two areas of potential impact arising from off-shore transmission networks, notably:

- Discrimination between international interconnections; and
- Effect on competition for new off-shore networks in NI.

### International interconnections

The island of Ireland is electrically connected to Great Britain through two interconnectors:

- **Moyle:** The HVDC Moyle Interconnector is the 500 MW HVDC link between South Ayrshire in Scotland and County Antrim in NI. This is owned and operated by Mutual Energy; and
- **EWIC:** EWIC (East West Interconnector) is a 500MW HVDC link between County Dublin and North Wales. This is owned and operated EirGrid Interconnector DAC – a subsidiary of EirGrid Group. EirGrid Group also own the Transmission System Operators for NI and the Republic of Ireland (SONI and EirGrid).

In addition to the above existing interconnectors, four further interconnections are in development:

- **Greenlink:** A new 500MW HVDC cable is under construction between Wexford in Republic of Ireland and Pembroke in Wales. This is planned to come into operation in 2024 and is owned by private equity;
- **Celtic Interconnector:** A proposed 700MW interconnector between Cork in Republic of Ireland and Brittany in France. This interconnector will be jointly owned by the Irish and French TSOs (EirGrid and RTE);
- **LirIC Interconnector Project:** A proposed new 700MW HVDC sub-sea electricity interconnector between the Belfast region and the Dumfries and Galloway region in Scotland; and
- **MaresConnect:** a proposed 750MW subsea and underground electricity interconnector system linking the electricity grids between the Dublin area and Denbighshire in GB.

The revenue models for the existing interconnectors (EWIC and Moyle) are similar:

- **Access Right Income:** All interconnectors earn money by transporting electricity. This money comes from selling access rights to those that trade

electricity – with that value (and hence price) of those rights strongly linked<sup>92</sup> to the difference in wholesale electricity prices at each end of the interconnector. For Moyle and EWIC, the relevant wholesale electricity prices will be the same – with both linking the wholesale markets for the SEM with the wholesale markets for GB.

- **Capacity Market Income:** Each interconnector contributes to security of supply for the island of Ireland by providing access to electricity from GB generators at times when there is insufficient electricity generation available on the island. This is recognised, with each interconnector receiving a payment through the SEM Capacity Remuneration Mechanism.
- **Regulation:** EWIC and Moyle are regulated by the relevant regulator (UR for Moyle, CRU for EWIC). The actual revenue (from the sale of access rights and from the Capacity Market) is determined by the relevant licence.
  - In NI the Cairt charge is the mechanism to make up any shortfall in Moyle required revenues or refund of any monies to consumers – with the difference flowing into the System Support Services tariff in NI; and
  - In Republic of Ireland the regulated costs are charged in transmission tariffs and facilitate profit to EirGrid plc as shareholder and a dividend to the Irish Government<sup>93</sup>

The stable and secure operation of the power system on the island of Ireland will occasionally mean that flows over interconnectors have to be adjusted. These adjustments will impact the revenue of the relevant interconnector.

Moyle is owned and operated by Mutual Energy. As a mutual company any over recovery can be returned to NI consumers. As it is not part of the EirGrid Group, Moyle has less visibility of why an adjustment to interconnector flows may be necessary.

In its response to the proposed SONI licence changes, Mutual Energy has noted: *“Our experience with SONI and EirGrid’s recent operational intervention in market determined NI to GB interconnector flows lacks transparency. In particular, it is not clear how SONI decisions are made and how NI customer’s best interests are reflected in those decisions versus RoI customer interests. We would expect scenarios like this to be better managed by a dedicated SONI team”*

### Offshore Transmission Networks

Offshore electricity generation<sup>94</sup> needs to be connected to the on-shore electricity networks to be of use. This is done through off-shore transmission networks.

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<sup>92</sup> There is a small adjustment to reflect transmission losses on the interconnector.

<sup>93</sup> <https://www.cru.ie/wp-content/uploads/2012/07/cer12149.pdf>

<sup>94</sup> At the moment, this is mainly offshore wind, but could also include wave power and off-shore solar

There are a number of elements of policy that will need to be developed for the development and management of off-shore transmission networks. At present, more of these policy elements have been established for the Republic of Ireland than for NI. As the respective policies develop:

- It is possible there could be a risk of compromised competition between competing providers of Offshore Transmission.

The Republic of Ireland has decided that all Offshore Transmission Networks in its waters will ultimately be owned and operated by the Republic's Transmission System Operator – EirGrid<sup>95</sup>. This policy has yet to be developed for NI, but may mirror that of GB where:

- Offshore Transmission is currently a competitive activity; and
- GB Government policy for the Future System Operator (FSO) suggest that, in the long run, Offshore Transmission will be planned by the FSO, and fall within its ambit for System Operation; however, the construction and ownership of that network may remain competitive.

Should NI Offshore Transmission Policy follow the path set by GB, there are several ways that SONI could act to distort competition amongst Offshore Transmission Operators (OFTOs) if governance changes are not implemented. This could include things that act to favour EirGrid as an OFTO over its competitors. Two potential examples are set out below:

- **Planning of Offshore network:** were SONI to take the role in NI that is envisaged for the FSO in GB, it would be planning the developments to the NI Offshore Transmission Network. It could design these in a way that the resulting projects played to the strengths of its sister company – EirGrid, such that EirGrid was then more likely to win those projects.
- **Connection Conditions:** There will be a number of specific technical requirements to be met where the Offshore Transmission Network connects to the existing on-shore network. These will be covered in a Connection Agreement between SONI and the relevant Offshore Network owner. The technical requirements of such an agreement are covered, in part, in the SONI Grid Code<sup>96</sup>, however this Grid Code has few specifics on the requirements for offshore connections – certainly compared to the specific requirements for generation connections. In practice, this means SONI will have a lot of discretion in setting these requirements on a case-by-case basis, with those requirements having an implication for the costs (and hence competitiveness) of the relevant project.

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<sup>95</sup> <https://www.gov.ie/en/publication/5ec24-policy-statement-on-the-framework-for-irelands-offshore-electricity-transmission-system/>

<sup>96</sup> [https://www.soni.ltd.uk/media/documents/SONI\\_GridCode\\_June2019.pdf](https://www.soni.ltd.uk/media/documents/SONI_GridCode_June2019.pdf)

An example of how connection requirements could be used to discriminate for or against specific projects relates to the requirements for Reactive Power provision. Offshore networks tend to be Direct Current rather than Alternating Current – meaning Reactive Power cannot be provided by plant within those networks. Instead, where the presence of an Offshore Network leads to a requirement for Reactive Power capability to maintain the quality and stability of the on-shore network – that capability would:

- Be built as an additional part of the equipment used to connect the offshore transmission to the onshore network; and
- That additional equipment would be part of the connection assets – funded by the Offshore Transmission Provider.

### **Treatment of the Electricity System Operator (ESO) in GB**

In November 2015, GB ministers called for greater independence for the ESO. This was in response to the evolution of the activities being performed by the ESO whose role was expected to continue to grow in importance. This created a need to *“carefully consider the governance of the ESO, to ensure that there is sufficient focus on its important role and to address any actual or perceived conflicts of interest between National Grid’s ESO functions and other business interests, such as the electricity TO and the electricity interconnectors”*. Whilst no evidence has been found that conflicts of interest have affected the work of National Grid’s ESO, OFGEM along with GB Government have now committed to establish a fully independent System Operator, which they refer to as the “Future System Operator” (FSO).

GB Government and OFGEM published a joint response<sup>97</sup> in April 2022 to their own consultation of July 2021 on the Future System Operator<sup>98</sup>. This re-confirms their commitment to a fully independent FSO covering all the roles of the current National Grid ESO as well as the roles of the GB gas Transmission System Operator in planning developments to its network. Key elements set out in the OFGEM/Government response include:

- **Consider Consumers:** The Future System Operator should be accountable to consumers. This is reflected in proposals for the FSO to have a statutory duty to have regard to impacts on consumers, and consumer behaviour.
- **State Owned:** The FSO will ultimately become state owned – albeit this needs primary legislation, and will wait until this can be accommodated in the

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<sup>97</sup> “Future System Operator, Government and OFGEM’s response to consultation”, OFGEM and Department for Business, Energy and Industrial Strategy, April 2022

<sup>98</sup> “Energy Future System Operator Consultation”, OFGEM and Department for Business, Energy and Industrial Strategy, July 2021

parliamentary timetable. This state ownership is related to the need for the FSO to be fully independent – notwithstanding that OFGEM and Government acknowledge the lack of evidence for actual conflicts of interest, or that such interests have led to any harm.

- **Advisory Role:** OFGEM and Government explicitly state the need for the FSO to have a mandated advisory role in a number of areas. In the main, this is driven for by the need for policy makers (OFGEM and Government) to have engineering advice in preparing policy to move to a Low Carbon economy. They explicitly state that:
  - The FSO's role makes it uniquely positioned to provide this advice; and
  - That the FSO's role in policy will be advisory only – with actual policy being the domain of OFGEM and/or Government.

Additional advisory roles are suggested – again being engineering nature. These relate to:

- Oversight and critique of plans for the development of energy networks – as submitted by the regulated owner/operators of those networks;
  - Oversight of electricity Distribution System Operators – and how they interact with the electricity transmission system; and
  - Planning for developments to the gas transmission network.
- **Government Strategy Statements:** The FSO will have to take account of relevant Government Strategy Statements – principally those relating to energy policy.

The July 2021 Consultation and April 2022 Government/OFGEM response to that consultation build on early consultations and policy decisions relating to electricity system operation in GB. Notably:

- The Electricity System Operator has already been set up as a separate company within the National Grid Group – with its own governance and licence. This followed an extensive programme of work and consultation started by OFGEM and Government in 2017 and involving National Grid Electricity Transmission (NGET), BEIS, OFGEM and the wider industry.
- The latest policy builds on the findings of a January 2021 consultation paper on GB System Operation. These four key findings are:
  - “Finding 1: Net Zero requires a step change in whole-system co-ordination and planning”;

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

The key separation arrangements arising from this earlier (2017 to 2019) work are:

- The ESO has a separate board with 3 National Grid Board Members, 3 Sufficiently Independent Directors<sup>99</sup> and a Chair who is the Director of the ESO;
- In principle, all ESO staff will be employed by the ESO with managers and executives incentivised on ESO metrics. (There is an exception for a small number of ‘dual fuel’ staff who will work for both the ESO and the gas SO);
- The ESO is physically separated from other parts of National Grid’s business;
- Transactional services are shared while strategic services will be shared under a business partner arrangement;
- The ESO has its own regulatory capability; and
- The ESO has a distinct visual identity to help to separate its culture from the rest of National Grid.

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

The key arrangements relating to physical, legal and staff separation were placed into ESO’s licence as part of Special Condition 2O, “Business separation requirements and compliance obligations, and conduct of the System Operator in performing its System Operator Functions”. In addition, Standard Condition B22 of the Transmission Licence was modified to increase the number of sufficiently Independent Directors to three.

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<sup>99</sup> As defined in Standard Condition B22 of the Transmission Licence: i.e. be a natural person with sufficient skills for the role and no executive position within the licensee’s business. Unless authorised by the Authority, it should not be an employee of, nor have a material relationship with, the licensee or any of its associates

We also note a review underway by OFGEM into the effectiveness of institutional and governance arrangements at a sub-national level to support delivery of net zero at least cost.<sup>100</sup> A number of options include potential new DSO roles for the FSO.

The significance with which this matter is being treated in GB is reflected in the fact that the UK Government is bringing forward legislation – Part 4 of the Energy Bill currently before the Westminster Parliament – to create the role of 'Independent System Operator and Planner' to enhance the remit and improve the governance of the existing GB System Operator. The future-facing role of the system operator in NI is no less important than in the other parts of the UK.

The extent to which NI government policy may wish to see something similar at the TSO and DSO level for NI is not clear at this stage.

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<sup>100</sup> <https://www.ofgem.gov.uk/publications/call-input-future-local-energy-institutions-and-governance>



## **Annex 6: SONI TSO in the SEM**

1. This annex explains how SONI and EirGrid TSOs should interact for SEM purposes and the key features of the regulatory framework for TSO interaction in the SEM.
2. Contrary to the position put forward by EirGrid/SONI, integration of the TSOs is not required for SEM. Instead the regulatory framework is predicated on collaboration between two independent TSOs who are required in their licences to either act in conjunction with one another or to cooperate with one another to deliver a range of TSO functions on an all-island basis. The policy goal is a single competitive wholesale market for electricity which benefits both NI and Irish consumers.

### **Policy intent on TSO interaction in the SEM**

3. The original vision of the two governments for the electricity and gas markets on the island of Ireland was set out in November 2004 in a framework document. The two governments envisaged a cross border energy market delivering long-term economic and social benefits that are mutually advantageous to NI and Republic of Ireland. The framework document set out a test against which the all-island energy market should be judged, and which was that 'energy users in both parts of the island are better off than they would be in two smaller markets which are mutually supportive good neighbours, but which trade together opportunistically rather than systematically.'
4. The framework envisaged 'unified regulatory and system operator arrangements for the island as a whole and geared to the delivery of measurable benefits.' In fact the unification of TSO arrangements for SEM was not progressed (see discussion on SEM legislation at Paragraph 7 below).
5. This vision was developed (as regards electricity only) and given expression in an inter-governmental memorandum of understanding (MOU) relating to the establishment and operation of a single wholesale electricity market in NI and Republic of Ireland.
6. Several aspects of the inter-governmental MOU are significant for present purposes because they recognise the potential for differences between NI and Republic of Ireland and that the SEM should be based on coordination between independent operators.
  - The MOU indicates that it was not the intention of the regulatory authorities to require harmonisation of all regulatory functions, i.e. that systems for the regulation of activities such as generation, transmission, and wholesale trading of electricity could differ between NI and Republic of Ireland.



- Secondly, the intention was that the SEM arrangements would ‘incorporate a harmonised approach to transmission connection policy and planning criteria for transmission networks and activities’ together with ‘appropriate regulatory and contractual arrangements for the planning, development, operation and contractual access for connection to and use of the transmission systems in NI and Republic of Ireland being undertaken on an appropriately coordinated all-island basis’.
  - In the interest of promoting competition it was intended that the SEM arrangements would include an ‘appropriately defined set of transmission system operator activities in each jurisdiction (including appropriate contractual arrangements in relation to the conduct thereof)’ and that the TSO activities would be separate from generation and supply.
7. The legislation for the SEM in NI and Republic of Ireland provided the legislative basis for the introduction of a single competitive market in electricity on the island of Ireland and facilitated the necessary licensing and contractual arrangements. The TSO activity in each jurisdiction would be separately licensed. In NI this entailed the development of a new TSO licence for SONI and separation of the TSO activity from NIE transmission and distribution activities. Significantly the legislation did not provide for the creation of a single system operator for electricity. The explanatory memorandum to the legislation in NI makes this explicit.<sup>101</sup>
  8. The TSO licence conditions of both SONI and EirGrid reflect this legislative intent as can be seen in the licence obligations on both TSOs to cooperate and act in conjunction with each other for SEM purposes (see further below). The licence also specifically provides for the contractual arrangements envisaged by the two governments, and in the case of the TSO activities this is the SOA.
  9. The SEM arrangements are therefore predicated on cooperation of two separate and independent TSOs, one in each jurisdiction, coordinating a number of their activities towards a common goal – a single competitive electricity market that is mutually advantageous to both NI and Irish electricity consumers.

### **Enabling TSO collaboration for SEM purposes**

10. This section outlines the legislative and licence requirements applicable to SONI TSO collaboration with EirGrid TSO for SEM purposes, including in regard to how the SOA should work. These arrangements are designed to ensure that consumers of electricity in Republic of Ireland and in NI, are protected and are not in any way disadvantaged in the SEM. We demonstrate how UR’s new

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<sup>101</sup> See Paragraph 11 of [Explanatory Memorandum to Electricity \(Single Wholesale Market\) \(Northern Ireland\) Order 2007 - Explanatory Memorandum \(legislation.gov.uk\)](#)

licence Condition 42 will further the legislative and legal requirements, and do so consistently with SEMC policy on the protection of Irish and NI consumers.

### *Legislative and licence requirements and the SOA*

11. The domestic electricity legislation refers to ‘consumers’ (e.g. meaning NI consumers in the Electricity NI Order) This reflects the fact that in accordance with legislation and the TSO licences they hold, each TSO only operates in its respective jurisdiction. EirGrid cannot legally operate as TSO in NI, and SONI cannot legally do so in Republic of Ireland.
12. Only the SEM Order refers to *‘the interests of consumers of electricity in Northern Ireland and Ireland,’*<sup>102</sup> and this reflects the fact for the purpose of the SEM the principal objective of the Department, UR, and the SEMC must include protecting the interests of both Irish and NI consumers.<sup>103</sup>
13. The TSOs’ licenses in each jurisdiction did not establish a ‘single system operator’. Instead the model requires certain system operation activities to be undertaken on an all-island basis jointly by the TSOs. For this reason EirGrid and SONI for SEM purposes have a duty (defined in their licences) to ‘act in conjunction’ with each other in relation to a number of TSO functions. This ensures that the NI and Irish transmission systems can be operated in a coordinated manner.
14. Acting in conjunction is defined in Condition 1, Paragraph 7 of SONI TSOs licence and mirrored in the EirGrid TSO licence. The definition means that where SONI is capable of fulfilling an all-island obligation without EirGrid’s assistance then it must fulfil the obligation.<sup>104</sup> But where it is not capable of fulfilling the obligation without EirGrid’s assistance then it must ensure that the SOA requires EirGrid to provide the assistance needed to SONI and SONI must exercise all the rights available to it to obtain the assistance needed, including where necessary amending the SOA. Similarly where EirGrid is obliged to act in conjunction with SONI, SONI must provide such assistance to EirGrid as needed to fulfil the obligation.<sup>105</sup>

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<sup>102</sup> While the Article 12 duties under the Energy Order do not include a general duty towards both sets of consumers, the security of supply duty does apply on a cross-border basis, even to the UR when it is just exercising its NI functions (see Art 12(2)(a)).

<sup>103</sup> For example, see principle objective of the Department, the UR, and the SEMC in relation to SEM as described in Art 9(1), The Electricity (Single Wholesale Market) (Northern Ireland) Order 2007.

<sup>104</sup> The condition states that SONI ‘shall use all reasonable endeavours to work together with the Republic of Ireland System Operator in so doing’.

<sup>105</sup> The SEMO licence also includes the same concept and it operates in the same way because UR and CRU each needed to be able to enforce the obligations on the SEMO licensed in their jurisdiction despite the fact that the model adopted for SEMO was based on a contractual joint venture approach in which either of the licensees might be relying upon the other to ensure the MO activity was being adequately carried out.

15. This concept is then reflected in a range of TSO licence conditions which require SONI to act “in conjunction with the Republic of Ireland System Operator”. These conditions include key TSO functions such as central dispatch, merit order and scheduling of generating units in the SEM (Condition 22, 22A), scheduling and dispatch within the balancing market (Condition 22B), capacity market arrangements (Condition 23A), Compliance and Assurance Officer (Condition 23B), the System Operator Agreement (Condition 24), reporting in dispatch balancing costs (Condition 39).
16. Several other licence conditions require cooperation with EirGrid TSO. For example, SONI TSO where appropriate, shall make arrangements for contracting for system support services in cooperation with EirGrid TSO (Condition 29 (Paragraph1)), and must cooperate with EirGrid TSO on the preparation of charging statements related to use of the all-island transmission networks (Condition 30).
17. The relationship between the two TSOs while ‘acting in conjunction,’ cooperating, or otherwise exchanging information with each other is governed by a System Operator Agreement (SOA). The EirGrid and SONI TSO licences require them to enter into, comply with, and at all times maintain in force a SOA (see Condition 24 of SONI’s TSO Licence). It governs their operational interactions with each other in respect to the carrying out of the TSO functions which must be coordinated for the purposes of the SEM, and this is a key document.
18. Moreover the SOA is fundamental to the ability of each regulator to enforce compliance with TSO functions in the SEM. Given that SONI and EirGrid are reliant on one another to carry out certain licence activities, the SOA needs to exist in order to ensure that those licence obligations will be complied with and can be enforced. It is SONI’s job to ensure contractually (through the SOA) that EirGrid does everything SONI needs to allow SONI to comply with their all-island licence obligations and vice versa. The purpose of the SOA is to provide SONI with a means of ensuring the EirGrid do those things SONI require for compliance (and vice versa) such that from UR’s perspective, SONI is directly responsible for its licence compliance even where it relies on EirGrid to do things to support such compliance.<sup>106</sup>
19. This concept of the SOA led to its governance – i.e. it is a document that is the responsibility of the TSO licensees (and not specifically endorsed by UR and CRU) and which the TSOs can modify by mutual consent. However it is also required by Condition 24, Paragraph 5, to include arrangements whereby disputes over changes can be referred to UR and CRU for binding determination.

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<sup>106</sup> The same model was used for the MOA.

## Protecting consumers following the acquisition of SONI by EirGrid

20. When SONI was acquired by EirGrid, ensuring that the interests of consumers of electricity in Republic of Ireland and NI were appropriately protected was a key driver for SEMC. To underpin this outcome SEMC recognised the importance of ‘acting in conjunction’ and of the SOA as an outworking of this concept.<sup>107</sup> SEMC envisaged the TSOs working together under the SOA such that each of them would essentially be mindful of the particular interests of consumers in their respective jurisdictions. Consequently SEMC agreed that the SOA licence condition should be amended, in both EirGrid and SONI TSO licences, to ensure that the SOA is designed to *‘at all times protect the interests of consumers of electricity in Northern Ireland and Ireland.’*
21. These changes were not about giving priority to one set of consumers over another, or about neglecting the interests of one set of consumers – they were aimed at maximising the interests of both sets of consumers. How the two TSOs interact is critical to this outcome. Each should bring knowledge of, and speak for, the needs of the consumers in their jurisdiction and cooperation or acting in conjunction under the SOA should enable SONI and EirGrid to reach conclusions which ensure that the overall outcomes from the SEM are a win-win for both sets of consumers.
22. This is not to say that each TSO should have a perspective which is exclusively jurisdictional but only that they are each expected to bring a jurisdictional perspective to TSO discussions, in order to agree the optimal way forward for NI and Irish consumers. The articulation of an effective SONI view may introduce a creative tension between SONI and EirGrid TSOs. However, this is healthy and the proper functioning of the system described above relies on structures, which allow any tension between jurisdictional perspectives to play out in joint TSO decision making.
23. Contrary to how the system should operate, SONI has stated that the “System Operator Agreement” between itself and EirGrid TSO has been ‘internalised’ in consequence of the shared operating model employed across the EirGrid Group. This internalisation of the SOA effectively renders it redundant and suggests an EirGrid view that legitimate differences between the transmission systems and operations of NI and Republic of Ireland are small or non-existent. Regardless of EirGrid’s preferences, the SOA was not meant to be ‘internalised’ between the two TSOs.

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<sup>107</sup> See SEM-08-176, Paragraphs 31 and 32.

24. We note that at acquisition, and as a further means to protect NI consumers, SEMC also decided to place a new obligation in Condition 3 of EirGrid's licence<sup>108</sup> so that when it is carrying out its regulatory functions it must at all times have regard to the interests of NI consumers as well as Irish consumers. Our governance decisions do not disturb this EirGrid licence condition and we consider the condition remains appropriate in circumstances where EirGrid continues to own SONI and as its shareholder can have some influence and where the UR's options facilitate a level of integration with EirGrid plc.
25. This condition in EirGrid's licence does not create a requirement for a corresponding condition in SONI's licence as SONI is the subsidiary company and is not in a position to influence EirGrid in the same way. The reference to Irish and NI consumers in SONI's licence inserted by SEMC is appropriately confined to the SOA licence condition as this deals with all-island coordination for SEM purposes. We do not consider that Condition 3 in EirGrid's licence is sufficient to address the concerns which we have identified in the course of this governance review – UR does not regulate EirGrid and cannot gauge the effectiveness of this condition. By the same token, CRU's statutory objectives relate to Republic of Ireland rather than NI.<sup>109</sup>

### **SEMC policy on SONI independence on acquisition by EirGrid**

26. SEMC policy at acquisition regarding SONI independence is outlined in SEM-08-176.<sup>110</sup> SEMC decided that regulatory measures were necessary in consequence of the acquisition of SONI by EirGrid plc. The aim of these measures was to ensure the removal or suspension of licence conditions that would preclude the acquisition and also modification of the independence conditions in SONI's licences.
27. These measures are relevant to SONI TSO's governance to the extent that they resulted in changes to SONI's licence conditions on independence and the formulation by SEMC of a general position on the independence which SONI should retain from EirGrid.

#### *Changes to SONI's licence conditions on 'independence'*

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<sup>108</sup> The changes to SONI's licence at acquisition were different to changes made to the EirGrid licence to ensure it acted in the interests of both consumers in NI and in Republic of Ireland. The change to SONI's licence included this obligation in respect of the design of the SOA only. The changes to EirGrid's TSO licence had wider effect, reflecting EirGrid's ownership of SONI.

<sup>109</sup> See Paragraph 2.11 of the Call for Evidence and Paragraph 3.69 of the January 2022 Licence Modification Consultation Paper.

<sup>110</sup> [SEM-08-176.PDF \(semcommittee.com\)](#)

28. A key concern of SEMC, as it considered issues related to the acquisition of SONI by EirGrid, was how to ensure that there was no vertical integration of electricity operators as this would be contrary to EU law and the principles of effective completion and open and transparent access to electricity markets. SEMC's immediate concern was that EirGrid's ultimate controller, the Irish state, also controlled ESB which engaged in the activities of generation and supply. SONI's pre-acquisition licence conditions on independence from generation and supply would catch the Irish state as EirGrid's ultimate controller and put SONI in breach of its licence once following the acquisition by EirGrid. This was not desirable given SEMC had previously accepted that state ownership of EirGrid and its role in the Irish electricity industry was not of concern to SEMC. SEMC desired an outcome which would retain the ongoing requirement for SONI independence from generation and supply while also relaxing certain requirements between EirGrid and SONI so that opportunities for economies of scale and potential for synergies and efficiencies between EirGrid and SONI could be realised.<sup>111</sup>
29. Consequently, the licence changes made by SEMC to facilitate the acquisition retained the general requirement for SONI independence from generation and supply (in compliance with the policy intent of the SEM and EU law) in the SONI licence conditions.<sup>112</sup> However, more relevant in the current governance context, the independence conditions of the SONI licences were also amended to remove the requirement for managerial independence of SONI from EirGrid. This allowed opportunities for economies of scale and potential for synergies and efficiencies to be pursued.
30. These licence changes reflected SEMC's view that SONI and EirGrid did not require the same degree of independence as had been necessary between SONI and NIE. As between EirGrid and SONI 'independence' remained important but could mean something less stringent. SEMC stated:
- 'The concept of independence remains important in terms of retaining SONI's corporate integrity and identity so that it should remain a standalone business with a specific role to play in the Northern Ireland transmission business.'*
31. Given UR's findings during the governance review it is clear that, contrary to the wishes of SEMC at acquisition, SONI's corporate identity and integrity and ability to remain a standalone business with a specific role to play has been undermined by changes to SONI's independence from EirGrid since acquisition in a manner which imposes risks to the protection of NI consumers.

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<sup>111</sup> See Paragraphs 24-28 of SEM-08-176.

<sup>112</sup> This is clearly the intention of SEMC – see Paragraph 27 of SEM-08-176.



32. More fundamentally these changes are contrary to the requirements of SONI's licence which requires it to be able to cooperate and act in conjunction with EirGrid as an independent TSO.
33. The changes to SONI's governance required by Condition 42 would tilt the balance of the relationship between EirGrid plc and SONI back towards ensuring a governance structure which is in line with good practice within corporate governance arrangements and the requirements of SONI's TSO licence.

### **Effect of Condition 42**

34. The changes to SONI's governance being implemented by UR do not change, in any way, the licence obligations requiring 'acting in conjunction', the requirement to have an SOA, nor the licence change in respect of the protection of Irish and NI consumers made by SEMC at acquisition.
35. The UR's licence changes are designed to maintain the TSO collaboration necessary to facilitate the SEM by ensuring the SOA works as intended and delivers increased transparency over TSO interactions. The new licence conditions also facilitate greater SONI independence at Board and management level as a prerequisite to allow SONI to develop and articulate the jurisdictional perspective envisaged by the existing licence conditions.
36. In particular Condition 42 will:
- a) Bring SONI TSO back into compliance with its licence obligations to collaborate, cooperate, and act in conjunction with EirGrid TSO.
  - b) Ensure transparency over TSO interactions such that UR and other stakeholders in NI can be assured that SONI is bringing an NI perspective to bear on TSO interactions under the SOA.
  - c) Open up TSO activities to regulatory scrutiny thereby ensuring licence compliance. Transparency of TSO interactions allows any problems to be revealed over time, enabling the SEMC or the UR, as appropriate, to take corrective action.
  - d) Facilitate SEMC and UR in each doing its job as greater transparency may highlight TSO decisions that SEMC may wish to call in as a SEM matter or the UR may wish to act on, if not called in by SEMC.
  - e) Ensure accountability by SONI for decision making on TSO functions which are coordinated with EirGrid for SEM purposes. TSO Governance must enable decision making between the TSOs which records how the balance

between the interests of the two different sets of customers had been struck, in particular where they are not aligned.

- f) Ensure that where SONI wishes to integrate with EirGrid for reasons that have nothing to do with SEM (example to secure efficiencies and economies of scale) that there is transparency over the arrangements with EirGrid, that they are in the best interests of NI consumers, and that these can be regulated effectively by UR.
- g) Proactively mitigate the risks for NI consumers which UR has identified in the current SONI TSO governance arrangements.

37. As desired by SEMC, the ability for economies of scale and synergies to be realised by SONI and EirGrid are retained in the new licence conditions. The condition facilitates sharing of resources with EirGrid by means of derogation from the general requirement for independence, provided the SONI Board can make an evidenced case to the UR to do so.

38. The ongoing licence requirement for SONI independence from generation and supply (reflected in Condition 12 of the SONI TSO licence) is not affected by the UR's new licence Condition 42.



## Annex 7: Worked examples of harm to transparency and the NI consumer interest

1. SONI and EirGrid have raised the objection that there is no evidence of actual harm. However, UR's concern is about the risk of harm and to protect the interests of consumers, not only by ensuring the absence of harm, but by optimising benefits to consumers by actively promoting improved outcomes for consumers. Accordingly UR does not always need to identify a source of harm before it can act. We have explained this in detail in the April 2021 Consultation Paper (at page 8) and in the January Licence Modification Consultation Paper at Paragraphs 3.67-3.68.
2. However, in any event, UR does consider that already there are some real-life examples of a lack of transparency (the "black box") in decision making related to SONI's functions and in relation to SONI's costs. There is also an example of the interests of NI consumers being overlooked.
3. **First**, in the approach to G-TUoS charging SONI's governance structures were not such as to bring SONI to proactively address an unjustified difference in treatment of internal costs which had resulted in a disadvantageous situation for NI stakeholders.
4. Condition 30 of the SONI TSO licence requires it to co-operate with EirGrid TSO to prepare charging statements. Among other things, the charging statement should set out the basis for charges for use of the All-island transmission networks to be levied on generators and suppliers in NI and any charges for system support services ("SSS"). The condition requires SONI to act 'in co-operation' with EirGrid.
5. In regard to the TUoS tariffs paid by generators, SEMC decisions form the basis of an all-island G-TUoS methodology, applied by the TSOs. The all-island G-TUoS charges will be levied on the basis of recovering 25% of the allowed revenue for 'network costs' on the island.
6. 60% of EirGrid's internal costs are being apportioned to Network Charges and the remaining 40% to System Services. The EirGrid approach has not changed since 07/08.
7. Any EirGrid internal costs which flow into the G-TUoS pot are paid for by all generators on the island, including those in NI. In 2018 UR raised queries with CRU as to why EirGrid TSO costs in relation to I-SEM were being recovered from G-TUoS tariffs given that no equivalent SONI costs were recovered via the G-TUoS tariff. In NI historically all SONI costs have been charged to NI consumers through the SSS tariff.

8. EirGrid allocating I-SEM costs to G-TUoS but SONI not would be in violation of the I-SEM Agreed Approach Document (ADD),<sup>113</sup> which specified costs to be split on a 75:25 basis. This is due to the fact that some EirGrid costs would be recovered from NI generators, but all SONI costs would be recovered from NI customers.
9. In 2014 SONI had gained responsibility for network planning from NIEN, largely aligning the responsibilities of the two TSOs in this regard. (EirGrid had been responsible for network planning in Republic of Ireland prior to 2014.)
10. However, SONI continued to recover all its internal TSO costs from NI users only through the SSS tariff while EirGrid continued to recover a proportion of its internal TSOs costs via the G-TUoS tariff. It would have been appropriate for SONI to question this to ensure fairness for NI users but it does not appear that SONI did so.
11. In 2019 following a large uplift in EirGrid costs being recovered through the G-TUoS tariff (due to I-SEM) UR raised queries with CRU as to why EirGrid internal TSO costs were flowing into the G-TuoS tariff and UR subsequently consulted on proposals to address this situation in 2019, eventually arriving at a solution to include a proportion of SONI internal TSO costs in the G-TUoS.
12. It is difficult to say which set of NI consumers the 'harm' falls on (demand or generation) as there were a couple of viable options to correct the misalignment. The point however is that additional costs were being charged to NI (in the form of EirGrid TSO costs) but this issue was not one which SONI thought to address. Rather, it fell to UR to take steps to do so.
13. The misalignment occurred across 7 tariff years from 2014-15 to 2020-21. The issue was resolved in April 2021 for application in 2021-22 tariffs. Assuming the final approach adopted in the G-TUoS decision paper is correct, SONI should have been allocating 15% of its internal TSO cost to the all-island generator pot over this period. Had this been the case, NI demand customers would have benefitted by approximately £17.4m in nominal terms. Assuming NI generators would have covered 25% of these costs via G-TUoS payments, NI as a jurisdiction has lost out by around £13m in nominal terms.<sup>114</sup>
14. If an independent SONI board had been in place we would have expected that when SONI gained responsibility for network planning it to 2014, the SONI Board and management would have questioned why SONI continued to recover all its internal TSO costs from NI users only through the SSS tariff whereas EirGrid continued to recover a proportion of its internal TSOs costs via the G-TUoS tariff. The G-TUoS tariff submissions are made to the regulators jointly with EirGrid

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<sup>113</sup> See the [ADD](#), p23, 4<sup>th</sup> bullet point.

<sup>114</sup> These figures are based on SSS tariff revenue for the years in question, excluding ancillary services and k-factor adjustments.

each year. Therefore there were opportunities for SONI board and management to review and question the figures and in particular to assess whether there was any misallocation of costs and any harm or unintended consequences as a result.

15. **Second**, SONI's position in the course of the development of the 2020-2025 Price Control was that SONI was unable to provide the UR with service area cost data.

16. As part of the price control Approach Decision the UR set out its intention to, *"introduce cost and service quality performance reporting for SONI's TSO activities"*. To that end, draft business plan data templates ("BDPT") were sent to SONI for consideration on 13 February 2019. The excel data template included Table 2 which was a new table for cost reporting by service area/activity. Although SONI made recommendations for changes to the BPDT on 07 March 2019, no changes were ever suggested to Table 2.

17. However, when the SONI business plan was submitted in October 2019, cost reporting by service area had not been undertaken. The explanation given by SONI in the plan was *"[t]his tab is not currently being completed due to the complexity of the calculations and the ever changing environment that the business finds itself evolving in. Explanation on this in the Roles and Services Chapter"*. In the Roles and Services Chapter (B.198 – B.199 of Appendix B to SONI's Business Plan), SONI commented:

*"B.198. SONI's internal cost centres and account codes do not precisely align with the split of our activities into roles and services. All of the services listed above are delivered by subsections of teams, with very few teams mapping directly to only one service. In addition to this, the continuing evolution of the roles of staff in teams and of teams themselves contribute to the difficulty in allocating costs on this basis in a structured and settled manner."*

*B.199. It is not be [sic] possible to provide any reliable information around the cost trends related to each service that would be accurate enough to base any decisions upon. It is certainly not possible to provide information to the standard appropriate for a regulatory price control submission, nor would the preparation of any such data be consistent with the standards of audited or auditable data which underpin the test [sic] of our submission."*

18. UR asked for the information again on a 'best endeavours' basis under the query log, explaining *"SONI has not completed this table in the BP submission due to complexity of the calculations. UR considers this to be very important detail as it helps to provide an understanding of the split of resource effort by*

*service/activity. Can SONI please attempt to provide this info on a best endeavours basis?"*

19. SONI's response was that *"SONI is not in a position to meaningfully attribute the costs on a Roles and Services basis under that table in any robust or auditable fashion."*
20. UR did not pursue this issue further, because it was clear that the information was not going to be forthcoming. Although it was possible for UR to progress the price control decisions without this detail (because overall cost and resource information was available) having an understanding of where resources are allocated within the business would have been very useful information, particularly in assessing areas where SONI was requesting cost uplifts.
21. Within Annex 4 of the Draft Determination relating to the Price Control (at Paragraph 4.16) UR explained that *"[t]he type of cost information that SONI currently reports for regulatory purposes is not sufficiently helpful in understanding the SONI's performance. For example, it does not provide much information on how the SONI's expenditure is distributed across the different activities and services it is engaged in."*
22. Indeed, the absence of such information was a barrier to SONI obtaining a benefit sharing framework which it had proposed. SONI's business plan had included a proposal for compensation based on *"the risks and costs associated with additional activities, including a premium for risk (which would proxy a competitive market outcome) to be linked not only to the value delivered but also the effort required to achieve it"*. However, without cost reporting by service area, SONI's proposals were not feasible. This was due to the fact that effort by area/activity was not transparent to the UR.
23. It was accepted that there would be some difficulty in completing this information as cost centre systems were not set up for service level reporting. However, this issue has obviously been complicated by virtue of the level of integration between the TSOs. SONI has alluded to as much when it pointed out the difficulty in allocating costs by service area due to continuing evolution of the roles of staff in teams and of teams themselves.
24. **Third**, and relatedly, later in the course of the development of the 2020-2025 price control, SONI was unable to provide even a breakdown of FTE staff.
25. A breakdown of staff roles was not initially requested in the business plan data templates used in the 2020-2025 price control. This was because of the original expectation that SONI would report costs by service area. As explained above, this did not happen because SONI said it was not possible.

26. Therefore, in an effort to provide assurance around the governance/challenge/efficiency of SONI's business plan, UR decided to conduct a 'deep-dive' audit of various projects.
27. In the course of discussions during this 'deep dive' audit, the issue of staff and reorganisation was raised. In particular, in the course of engagement between UR & SONI between the Draft and Final Determination, the issue of a staff resource profile was discussed and requested on various occasions. SONI explained, for example at a meeting on 11 August 2020, that a restructuring was taking place, which made the information more difficult to provide. However, the UR indicated at that meeting and in the email summary of actions sent after it that it would be interested to see even a point in time picture of staff as at the date of the Business Plan submission. At subsequent meetings, for example on 27 August 2020, the UR explained that it had a concern about transparency and encouraged SONI to submit a resource plan for Full Time Equivalents (FTEs). On 4 September 2020, the UR explained that SONI is an organisation whose services are all based around its people so it was considered proportionate to ask for a resource plan.
28. Ultimately, this issue was not pursued further because it had become apparent to the UR that the information would not be forthcoming. Although it was possible for the UR to progress price control decisions without this detail (because the UR had overall cost and resource information available), not having a staff resource map:
- i.* Had a significant resource impact for UR and SONI in terms of the number of meetings and queries to discuss and clarify confusion around the number of FTEs being requested; and
  - ii.* Meant that the UR had little scope for challenging the efficiency of base costs as the split of resource by service area was not known. Benchmarking of TSOs is also limited to wage rate comparisons. Therefore UR had no basis to challenge the number of existing staff employed. UR had also limited context to consider the need for additional staff resources requested by project. This was due to the fact that extant resources by work area was not known.
29. The consequence was that UR had to make decisions and assumptions based on imperfect information. In some respects, lack of transparency also hindered the SONI case for additional resources. This was due to the fact that UR was unaware of the current staff compliment in a service area so could not make a clear distinction if the number of uplifted staff was reasonable.
30. In a similar fashion, this lack of detail also made benchmarking of staff salaries more problematic. Without details of staff roles, UR was obligated to accept the staff role splits as set out in a KPMG report prepared for the business plan. Whilst these ASHE (Annual Survey of Hours & Earnings) comparators and percentage

splits may be reasonable, UR has no way to confirm this is so without the relevant staff detail.

31. **Fourth**, this absence of transparency has made the consideration of requests for funding under the uncertainty mechanism more difficult. For example, the UR did not provide funding requested in the SONI Business Plan for the 2020-2025 Price Control for replacement of the IT systems used to collect, collate and analyse meter data because the scope and costs remained uncertain. SONI has now made an uncertainty mechanism claim for this project. The request is still being assessed by UR, but the UR considers that the absence of staff and resource information makes this assessment much more difficult. By reason of the fact that UR does not have sight of what internal resources are engaged in it is difficult for UR to understand whether SONI has internal resource available or not, and therefore whether there is justification for the use of higher external costs.