

Kevin O'Neill
SONI Limited
Castlereagh House
12 Manse Road
Belfast
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Ref: NET/E/PR/927

23 April 2024

Dear Kevin,

Re: SONI Governance Phase II (Mobilisation) – Final Dt approval

Thank you for the opex *Dt* submission of the 05 January 2024 regarding mobilisation costs associated with Phase II of the Governance project. In addition to the request, a paper on the *SONI Governance Approach to Funding* was provided on the 31 January 2024. This final approval letter considers both the requested allowance and the approach to funding future phases.

UR provisionally approved a budget of **£974k (Jan 2024 prices)** on 15 March 2024 for Phase II, setting out the conditions for approval. SONI made representation to the UR on 27 March 2024. Following review of this response, UR has determined a final *Dt* allowance under Annex 1, paragraph 8.6(a) of the licence for **£974k (Jan 2024 prices)** in line with the provisional decision.

For confirmation, amounts finally approved are detailed in the table below by tariff year [and in April 2019 prices for ease of comparison with the current price control].

Tariff Year	SONI Claim (Jan 2024 prices)	UR Allowance (Jan 2024 prices)	UR Allowance (April 2019 prices)
2023-24	£974.0k	£974.0k	£806.2k
Total	£974.0k	£974.0k	£806.2k

Conditions of Approval

The funding paper has requested future submissions based on high level outputs and VROM cost estimates. SONI has also suggested enhanced cost reporting and cited the Future System Operator (FSO) model by way of precedent.

Full details on our thoughts to SONI views on the approval conditions are set out as an annex to this letter. However, we are not minded to amend the conditions set out in the PD

letter. These conditions on both the future funding approach and the Phase II allowance are as follows:

- 1) We recognise that SONI has, of necessity, formulated the submission in the context of a high degree of uncertainty and this makes it difficult for SONI to justify the upper end figure of £974k, and for UR to have confidence in that figure for the mobilisation phase. We expect this level of allowance to cover a substantial amount, if not all, of the activity in the *Design and Plan* Phase. Consequently, the allowance of £974k is on the basis that the activities and outputs will be rescope by SONI for UR review when better information is available (as discussed under point 4a below).
- 2) Approval of the £974k cap should not be considered as endorsement of staff recruitment plans or daily consultancy rates for the implementation of condition 42.
- 3) We recognise a desire on the TSO's part to increase the resources and expertise in SONI. We are willing to consider additional resources for SONI, but would rather do so holistically as part of an overall vision and resource plan for SONI, which takes account of the role of shared services in the future.
- 4) We welcome SONI's proposals for more reporting (as per the SONI funding paper). This should include the following activity:
 - a) Within a month of starting, we expect a report on what will be delivered with the initial funding and expectations for the full plan of work.
 - b) As part of regular reporting, we expect an updated schedule at the end of each month which shows a developing plan. At phase end we would expect a proposal for the *Design and Plan* phase for our review.
 - c) We also expect SONI to provide a more detailed timetable and milestones for the programme, including best estimate for timing of derogation applications.
 - d) We expect SONI to focus on deliverables which would not be nugatory regardless of the final extent of derogation applications.
 - e) Reporting should include monthly updates on spend and activity.
- 5) Regular reporting should begin immediately. As discussed with SONI, we will need a detailed timeline (point 4c) from SONI, including when SONI will be able to submit any derogation applications. We understand that all the information to develop this is not available at present. However, we need a timeline with as much detail as possible to be submitted by 31 May 2024 at the latest. This is necessary to understand the scope of work for the implementation phase.
- 6) We expect an ex-post review of costs will be undertaken (either by UR or an independent consultant) on project completion. As part of this SONI should furnish all relevant details to allow completion of the review i.e. vendor lists / invoices / consultant timesheets / daily rates / activity & outputs / reports / internal staff use, etc.
- 7) Our expectation is that SONI's reliance on VROM estimates should decrease as the programme goes forward. If the level of certainty does not increase, there will likely

need to be a pause to allow detailed review of the implementation phase submission following the detailed design work.

- 8) A pause may also be needed depending on the magnitude of future requests for allowances and in circumstances where UR may need to engage its own specialist support to assess future requests.
- 9) In order to protect customers, we are considering treating all phases and spend associated with the governance project as opex (as per the FSO example cited by SONI in the funding paper).

By way of a longer-term issue, if consumers are going to be exposed to VROM risks going forward, it may be that a change to the DIWE mechanism should be considered. This change might include making ex-post reviews and decisions a more common part of the uncertainty mechanism process. This issue may merit further consideration.

I trust this satisfies your requirements at this time.

Yours sincerely,



Peter Russell
Executive Director
Price Control, Networks, and Energy Futures

Annex A – UR views on SONI’s Approval Condition Points

SONI has provided a detailed response to the UR provisional decision regarding the SONI Governance Phase II project conditions of approval. UR views on the SONI comments are set out in the table below.

	SONI views and UR Responses
SONI Comment	SONI cannot confirm at this stage whether the provisional funding will be sufficient to cover all or a substantial element of the <i>Design and Plan</i> Phase. We will work closely with the UR to determine the impact on the initial approval and whether an uplift may be needed. The Dt mechanism allows for uplifts to be progressed based on a clear scope and need.
UR Response	<p>This engagement is welcome. However, our expectation remains that the level of funding should be sufficient to cover a substantial amount, if not all, of the activity in the <i>Design and Plan</i> Phase.</p> <p>This conclusion is based on the analysis of high-level outputs provided and the level of external consultancy support necessary to deliver detailed business planning change i.e. external consultancy support costs for price controls.</p>
SONI Comment	SONI is unclear on this statement [<i>that approval of the £974k cap should not be considered as endorsement of staff recruitment plans or daily consultancy rates</i>]. We would welcome engagement on what evidence is needed that we have not provided.
UR Response	<p>As per condition 3 in the PD letter, we would wish to make decisions on the new organisational structure holistically as part of an overall vision. Hence the need for a derogation timeline by the end of May 2024 and detail on the resource plan before implementation cost requests are submitted.</p> <p>This statement simply confirms that we are not endorsing the staff recruitment plans or daily consultancy rates at this time. To do so, the evidence required would include a view of the new organisational structure, resource plans, areas of joint working, justification for new recruitment, activities of consultants etc.</p> <p>SONI is already recruiting the senior management posts in its new structure. We recognise that SONI will need to increase its management capability, but the efficient level will need to be assessed as part of an overall resource plan for SONI. In regard to recruitment underway, SONI will need to demonstrate that these posts will be needed irrespective of the future operating model.</p>

SONI Comment	<p>SONI agrees with this approach. As we have communicated, we are actively engaging with EirGrid on how the two TSOs can work together in the future. This work needs to be completed on order to allow SONI to finalise its resource plan. SONI proposes the following approach in terms of resourcing:</p> <ol style="list-style-type: none"> 1) SONI to build up a full resource plan based on its new organisational structure, as approved by the SONI Board. This will need to include any 'working together' arrangements with EirGrid. 2) SONI to determine the phasing of when functions will be fully independent/new arrangements are in place. 3) SONI to determine the overlap period where company recharges will continue to apply while the new SONI teams are established and a controlled handover is managed. 4) SONI to present the resource plan to the UR which demonstrates the uplift in resources needed and the timing of this change programme. 5) SONI to demonstrate the comparison of costs vs existing allowances and seek approval for any incremental costs above exiting allowances. This will include a transparent justification for the increase in headcount. <p>SONI is dependent on EirGrid in order to complete this work and are treating it as a priority area.</p>
UR Response	<p>This approach is welcome. The approval condition remains unchanged. Detail should be provided before implementation cost requests are submitted.</p>
SONI Comment	<p>We are targeting having this information [<i>report on what will be delivered with the initial funding and expectations for the full plan of work</i>] available at the end of the mobilisation phase. We would expect to be in a position to share this with the UR in late April.</p>
UR Response	<p>This assurance is welcome. The approval condition remains unchanged.</p>
SONI Comment	<p>We are planning that we provide a monthly update to the UR following on from each SONI Board meeting. A report could be provided on the second Friday of each month. We will be working on having a funding request prepared at the end of the mobilisation phase.</p>
UR Response	<p>Commitment to a monthly update is appreciated. The approval condition remains unchanged. However, we would not expect a further funding request until a material proportion of the <i>Design and Plan</i> phase has been completed.</p>
SONI Comment	<p>We are unclear what this statement [<i>regarding nugatory spend</i>] means. SONI would welcome further engagement on this point.</p>
UR Response	<p>This is simply a reference to ensure the focus is on areas where spend is fully justified. As made clear by the Phase I allowance, "<i>while Condition 42 does not prevent a full demerger, it certainly does not mandate it.</i>" Accordingly, any cost incurred in pursuing areas for full independence without justification may be subject to DIWE review.</p>
SONI Comment	<p>SONI will propose a reporting template for the monthly reports and share with the UR.</p>

UR Response	This will be a useful way to proceed. The approval condition remains unchanged. We would welcome confirmation on when this reporting template will be provided.
SONI Comment	SONI will work towards having a plan submitted by end May 2024 based on the best information available to us at that point in time.
UR Response	We agree with this commitment. The approval condition remains unchanged. However, we would stress the importance of providing as much detail as possible on the derogation process in order for the UR to understand the scope of work for the implementation phase.
SONI Comment	<p>We are unclear on the purpose of the ex-post review. We would expect that the UR will have sufficient information throughout the project and be able to flag any concerns at that time rather than ex-post.</p> <p>The SONI price control does not include an ex-post review function. It does however have DIWE functions. We would welcome clarity whether this is what the UR mean when it says it expects to undertake an ex-post review. SONI would welcome further engagement on this point.</p>
UR Response	<p>The purpose of the ex-post review is to provide assurance that costs have been properly incurred. This is a common regulatory approach where VROM allowances are provided. Whilst additional reporting is helpful, we do not anticipate that it will provide the necessary level of assurance required.</p> <p>We would note that the UM Guidance (para 7.2) does actually allow for further information requests and third party audits. This is not typically undertaken but seems appropriate in this instance where VROM allowances have been requested and additional monies are expected to deliver similar outputs. Ultimately, the ex-post review will help determine whether a DIWE process needs to be followed.</p> <p>The approval condition remains unchanged to provide SONI early understanding on the approach and what information will be required to complete the review.</p>
SONI Comment	<p>SONI considers that the engagement with EirGrid and clarity on how the two TSOs with work together in the future is a key prerequisite for the implementation phases.</p> <p>SONI has structured the programme to allow some areas that are considered by the SONI Board as fully independent to be progressed (subject to funding approvals) as separate phases.</p>
UR Response	<p>We agree that the approach to TSO joint working is a key prerequisite for the implementation phase. The approval condition therefore remains unchanged.</p> <p>However, we would wish to make decisions on the new organisational structure holistically as part of an overall vision. Hence the need for a derogation timeline by the end of May 2024 and detail on the resource plan before implementation cost requests are submitted.</p>
SONI Comment	SONI understands this need <i>[for a review pause]</i> . SONI requests that any pauses are signalled early such that SONI can manage its internal and external resourcing accordingly. In addition, SONI expects that the UR would reflect any pauses in the durations and dates set out in LC42 via directions.

UR Response	We will endeavour to provide early signals where a review pause is required. However, this will be dependent on the quality of information provided by the TSO in its submissions.
SONI Comment	<p>SONI expects that programme costs should follow accounting rules and the revenue treatment would follow these rules. The funding sought to date is all opex, however, there may be costs in the implementation phases that may need to be treated as capex (e.g. new IT systems).</p> <p>SONI would welcome engagement with the UR on this point. Depending on the scale of the costs for implementation, treating all costs as opex may have a material impact on tariffs.</p>
UR Response	<p>This issue will be determined on a stage-by-stage basis. As such, the approval condition remains unchanged. Its purpose is to provide an early signal that SONI should <u>not necessarily expect</u> regulatory revenue treatment to follow existing accounting rules in this instance (though this can be discussed).</p> <p>Whilst it is accepted that opex treatment may have a material impact on SSS tariffs, the electricity bill impact should be relatively limited. It would also follow the FSO precedent and avoid the drawbacks of the capex up-to-a-cap framework (as specified in the UR letter to SONI on 06 December 2022).</p>
SONI Comment	The SONI price control does not include an ex-post review function. It does however have DIWE functions. Any changes to the DIWE mechanism would require public consultation. Note that this mechanism also applies to NIE Networks.
UR Response	We would note that the UM Guidance (para 7.2) does actually allow for further information requests and third party audits of ex-post costs. However, we agree that any changes to the UM framework would require public consultation.