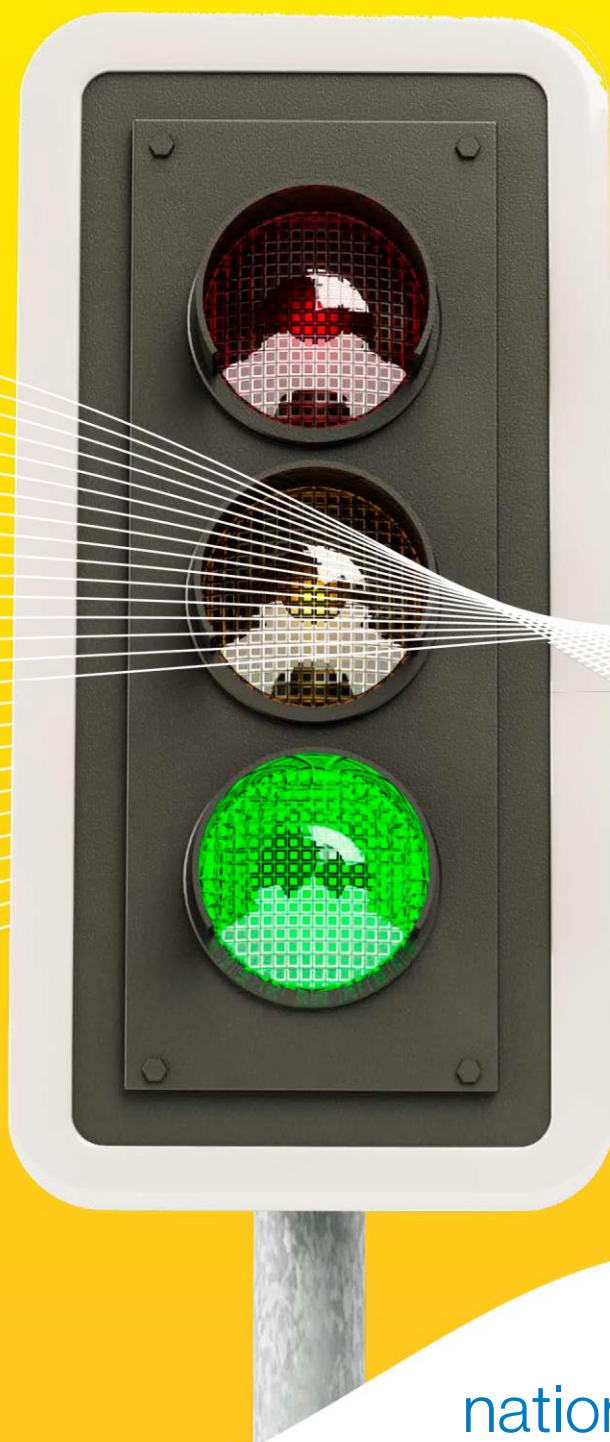


# National Grid Electricity System Operator Business Separation Compliance Statement

Version 1.3, July 2020



nationalgridESO

# Foreword



**From Fintan Slye,**  
Director Electricity System Operator

## Why does the ESO need to be more independent?

Competitive marketplaces, supported by smart system operation, will ensure efficient use of all energy resources wherever they sit in the UK's energy system. Consumers stand to benefit from the sustainable energy transformation that is facing the energy sector and the ESO has new roles to play in facilitating this transition.

The changing nature of generation, particularly the increase in small generation connected at the distribution level, has highlighted the need for a more holistic and coordinated approach to planning and operating the electricity transmission and distribution systems. To be effective in delivering these new roles, the ESO must be trusted to be neutral and impartial. Perceptions of conflicts of interest between the ESO and the transmission and asset-owning parts of the National Grid portfolio could damage this trust. Legal separation addresses and solves this challenge.

## What has changed?

National Grid's portfolio of businesses already had business separation in place; all licensees were prohibited from unfairly advantaging each other. However, National Grid Group realised that, because of the unique position the ESO has in the UK's energy system, it needed to go further. To give the ESO more independence and to create that trusted, impartial organisation, the ESO needed its own licence, separate from the electricity transmission owner, and its own board with strong, independent oversight and clearer separation from the influence of the rest of the Group.

## How will we measure the success of this change?

This compliance statement describes how we have set up the ESO. The statement is complemented by the annual compliance report, which is produced by the ESO's Compliance Committee, chaired by Paul Plummer, a Non-Executive Director of the ESO.

The Compliance Committee will scrutinise and evaluate the design and implementation of the legally separate ESO; bringing challenge and advice to the ESO to ensure we are demonstrating our increased independence and neutrality in all our actions.

The Committee will use their Annual Report and an ongoing dialogue with Ofgem to share their perspectives on how we have progressed. The Annual Report will set out how we have delivered compliance in each of the areas that this statement covers. The report will highlight any business separation compliance weaknesses, and what we are doing to rectify them.

Together, these documents are an important part of demonstrating the creation of a more independent and neutral ESO. If we are successful, delivering complete transparency around how we operate as a legally separate entity will build trust with customers and stakeholders and allow us to successfully step up and take on new roles in driving forward the sustainable energy transformation. In turn, our success will be reflected in how our performance is measured by customers and stakeholders throughout the year.

# Executive summary

The compliance statement is a requirement of the electricity system operator's (ESO) licence. It sets out the practices, procedures and systems which the ESO has adopted (or intends to adopt) to ensure that it is compliant with the business separation requirements set out in Special Condition 20 of its licence.

This executive summary is a high-level description of what the ESO has changed and implemented to achieve compliance with the licence obligations.

## ESO governance & interactions with National Grid Group

ESO has autonomy in decision making on matters related to its licensed duties and the day-to-day operation of the ESO business in accordance with its Articles of Association and Reserved Matters. It is governed by its own board of directors with three Non-Executive Directors (NEDs) and four ESO Directors.

As a subsidiary of National Grid Group, the ESO needs to interact with the Group. To support operational and managerial separation of the ESO, and independence of the ESO Board, a new Group level committee, the ESO Committee, has been established. The ESO Committee ensures all ESO ringfenced information that is required to support good corporate governance is viewed separately from other subsidiaries in the National Grid Group. The ESO Committee is not involved in the day-to-day operation of the ESO.

## Financial requirements

To ensure no cross-subsidy between the ESO and any other National Grid Group entities, the ESO has its own, separate accounts. The ESO's statutory accounts will be published in 2020 and subject to external audit.

The ESO has robust debt management, sufficient working capital arrangements and potential financial assistance from the National Grid Group. This corporate financial structure has resulted in the ESO gaining an investment grade credit rating.

## Operational separation

To enable operational separation of the ESO from the electricity transmission owner (ETO), industry codes were modified using the relevant code governance arrangements. The modifications clarified the responsibilities and accountabilities for operational activities and commercial arrangements between the ESO and ETO, and ESO and other code parties to reflect the new legal entity and align the new relationship with the ETO with other TOs.

To comply with the updated industry regulatory framework, the ESO and ETO have reviewed all their internal business procedures and processes.

The electricity and gas system operators previously operated with a dual fuel leadership team since the NG-Lattice merger in 2002. Following legal separation in April 2019 we retained a single OneSO structure, comprising the GSO and ESO but on further review it was decided that from 1 January 2020 the ESO and GSO would be managed separately. The changes provide necessary clarity for our employees and external stakeholders and make the legal separation of the ESO even clearer.

On June 8<sup>th</sup> 2020 the Director of ESO's reporting line changed from the UK Executive Director to the Chief Executive of National Grid Plc. As a part of these changes the UK Executive Director stood down from ESO Committee and the Director of ESO stood down from the UK Executive. ESO will continue involvement in broader Group interests such as Talent management, SHE and Ethics and Compliance.

Legal separation of the ESO has also strengthened the barriers between the ESO and National Grid Gas and National Grid's non-regulated businesses.

## Information ringfencing

Information ringfencing refers to the protection of ESO information ("System Operator Functions Information", SOFI). It is important that parties should only have access to the SOFI that they need to be able to deliver their licence requirements and fulfil their roles.

To enable the ESO to continue to operate effectively as well as comply with the SOFI protection rules, the ESO has updated its systems and unstructured data with appropriate access controls and restrictions, reviewed and redesigned its processes and ways of working, and trained its employees on the new obligations.

Exemptions to the information ringfence obligations allow sharing of information between the ESO and other National Grid parties (e.g. the ETO, the shareholder, shared services teams working for the ESO etc) in specific, legitimate circumstances. The ESO and the receiving party have introduced controls to protect SOFI when it is shared through these legitimate routes.

## Employee transfer, moves and talent management

Controlling and monitoring the movement of employees ensures that the ESO has the capabilities that it needs,



and that all aspects of business separation are appropriately observed when individuals leave the ESO.

Employees undertaking ESO activities are contractually aligned to the ESO. Any new starter to the ESO receives an induction and undertakes business separation training to ensure they understand the business, their role and their compliance obligations. Employees moving to any other National Grid entities are subject to the review of the Business Separation Compliance Officer who determines whether special measures are needed to maintain compliance.

The ESO Board has visibility of the process and plans for all ESO Senior Leadership as well as sight of the ESO's strategic workforce planning, diversity and inclusion strategy. The ESO business has autonomy in capability development and recruitment and benefits from access to the National Grid Group's talent pool and talent development opportunities.

### **Employee incentivisation, reward and remuneration**

The ESO has made changes to the financial and business measures underpinning how ESO employees are incentivised and rewarded for their performance. The revised measures ensure that ESO employees are only incentivised on ESO performance.

### **Visual identity**

The ESO has created a new ESO identity and brand to establish a lasting change for the business, employees, customers and stakeholders. This includes transforming its physical appearance through new logos, imagery and colour palettes and the way its employees present and identify themselves through changing its behaviours and culture.

Its new brand and identity differentiate the ESO from the rest of the National Grid businesses whilst maintaining the brand recognition of National Grid Group as a supportive parent company.

### **Physical separation**

The ESO has changed the physical arrangements for its workspace to help drive the cultural change around legal separation and support other aspects of separation like compliance with the new information ringfence. It has created a new, physically separate office for ESO employees in Warwick called Faraday House.

The ESO has relocated any employees who are directly or solely working for NGET or NGG from its Wokingham site which is the location of the Electricity National Control Centre.

Any National Grid employees outside the ESO or its shared service providers visiting these buildings will be identified and treated the same as an external visitor.

### **Cross fuel insights**

The energy industry is in a rapid transition period as it moves towards a decarbonised, decentralised and digitised world. Whole energy system thinking is increasingly important, but National Grid Group must also demonstrate that it has created a more independent ESO, that is separate from the asset-owning focus of the other parts of National Grid Group, including National Grid Gas. As such the ESO operates separately, but will collaborate alongside other market participants to deliver the whole energy system agenda.

### **Shared services**

National Grid Group operates a shared service model whereby some support functions are shared between the subsidiaries of the National Grid Group. The ESO licence allows this model to continue, with some additional rules and restrictions for ESO shared services to comply with.

National Grid Group has reviewed and assessed the processes for all the shared services functions and redesigned processes, changed ways of working, organisational structure and implemented access controls and restrictions within its shared services teams to ensure they can provide support compliant with the ESO licence.

The Group's Finance, Corporate Affairs, Legal, Human Resources (HR), Information Technology (IT) shared services functions have put in place a dedicated business partner (and are members of the ESO Executive Team) to deliver the strategic activities which they provide to the ESO, transactional activities continue to be provided by teams that are shared with other entities in the Group.

### **Compliance Committee and Business Separation Compliance Officer**

The ESO has appointed a Compliance Officer to facilitate its business separation compliance. The Business Separation Compliance Officer is not involved in the management or operation of the system operator functions. They report to the ESO's legal business partner.

A member of the ESO Board has also been appointed as Single Appointed Director to oversee the duties and tasks of the Business Separation Compliance Officer.

A Compliance Committee has been established as a sub-committee of the ESO Board to oversee the ESO's compliance against its business separation obligations. The Committee is chaired by a NED.

More details on the above compliance requirements are provided in each relevant chapter and the appendices contain supporting information and evidence for various parts of the statement.

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# 1. Introduction

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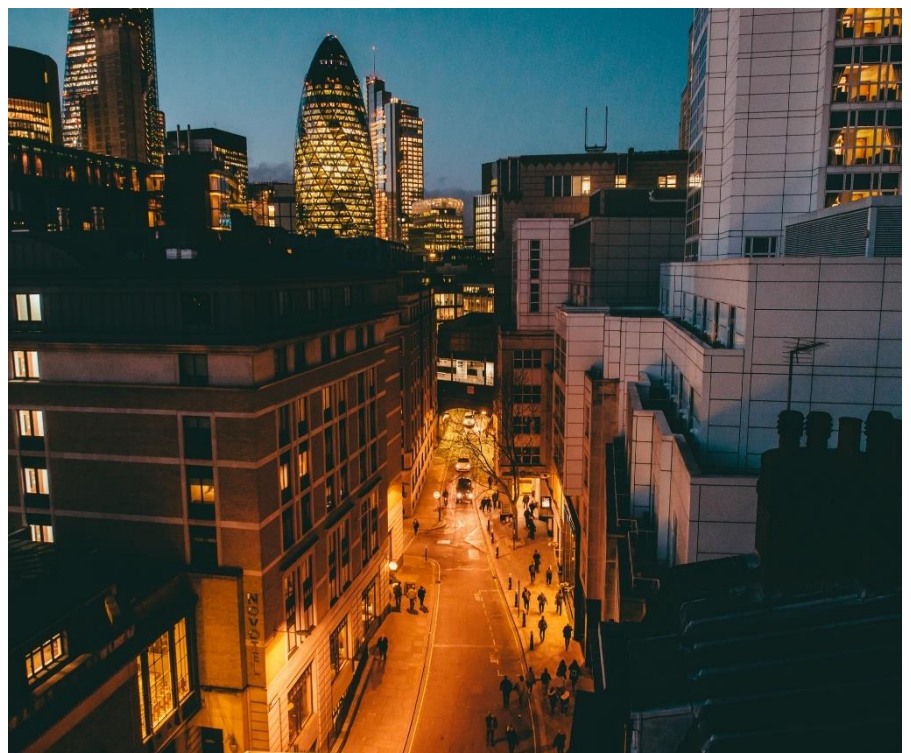
## What is this document?

This document is a requirement of the electricity system operator's (ESO) licence. It sets out the practices, procedures and systems which the ESO has adopted (or intends to adopt) to ensure that the ESO is compliant with the business separation requirements set out in Special Condition 20 of its licence.

This compliance statement also describes how the ESO has achieved the objectives of legal separation to create a legally, financially, managerially and operationally separate entity from NGET and the other National Grid businesses.

The aim is to make this document as descriptive, readable and accessible as possible, so that the separate governance, decision making and day-to-day operation of the ESO is open and transparent to customers, stakeholders and the regulator.

This statement has been approved by the ESO Board and Ofgem. It will be reviewed on an annual basis to provide an update on the compliance controls the ESO has put in place. The ESO also submits an Annual Compliance Report to Ofgem to demonstrate compliance with Special Condition 20, business separation and compliance obligations, of its electricity transmission licence.



# 1. Introduction

## The ESO's compliance culture

The ESO has a unique position as the system operator of the Great Britain (GB) electricity transmission network, as such it operates under strict regulatory and legal rules. A strong compliance culture is therefore firmly embedded in the organisation, with robust compliance controls in place for our existing licence obligations.

In addition, all employees are expected to comply with the Code of Ethical Business Conduct and complete mandatory computer-based training in modules of Business Separation (from National Grid's other businesses), Competition Law, Fraud and Bribery, Ethics and Data Management.

National Grid Group's core company values of 'do the right thing' and 'find a better way' guide all employees' behaviour. All parts of National Grid Group take pride in the organisation's reputation for working responsibly with customers, colleagues and consumers.

## Ensuring compliance with our new obligations

Building on this strong compliance culture and framework, the new ESO licence includes additional business separation obligations. Because of this change, the ESO has assessed its people, processes and systems and implemented changes and new controls as needed.

These changes focus on designing a compliant environment for the ESO to operate in, as well as implementing controls to maintain compliance on an enduring basis.

All ESO employees signed a Personal Compliance Declaration (Appendix 2a) to confirm that they and the employees in their teams have completed the relevant business separation training and are able to carry out their roles compliant with the new legal separation rules by having implemented the required changes in their teams.

The enduring control framework is explained in Appendix 3.

## How is this document structured?

Each chapter covers one of the business separation requirements as defined by the ESO licence. The chapters are ordered as below:

- ESO governance & managerial separation
- Corporate governance
- Financial requirements
- Operational separation
- Information ringfencing
- Employee transfer, moves and talent management
- Employee incentivisation, reward and & remuneration
- Visual identity
- Physical separation
- Shared services

The final chapter describes the role of the ESO Business Separation Compliance Officer and Compliance Committee.

In each chapter, we use a generic structure setting out:

- **Licence requirement** – the exact text from Section 20 of the ESO licence.
- **Summary** – an overview of what the compliance theme is and how the ESO has achieved compliance.
- **Compliance theme** – what the compliance theme is and why it's a requirement of business separation.
- **Compliance design** – what the ESO has changed to become compliant and what controls are in place to maintain and assure compliance on an ongoing basis.

The appendices contain supporting information and evidence for various parts of this statement.



## 2. ESO governance & managerial separation

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# 2. ESO governance & managerial separation

## 20 Part B and 20.20 (b) (i)

The ESO must ensure it is legally and functionally separate from NGET/NGG/ROCB and confirm the arrangements for managerial and operational separation including arrangements to ensure the independence of the licensee's management board, senior managers and staff from NGET, NGG and ROCB.

### Summary

National Grid Electricity System Operator Limited (NGESO Limited) is a legally separate entity within the National Grid Group performing the electricity system operator (ESO) role in Great Britain. NGESO has autonomy in decision making on matters related to its licensed duties and the day-to-day operation of the ESO business in accordance with its Articles of Association and Reserved Matters. It is governed by its own board of directors with at least three Non-Executive Directors (NEDs).

The ESO Executive Team has delegated authority from the ESO Board, creating an operating model, capable of providing additional value to consumers through delivering Whole System thinking.

### Compliance theme

Corporate governance is the system by which a company is directed and controlled. For the new ESO company, this relates to the arrangements of the new ESO Board, its terms of reference and how it interacts with the ESO business. Arrangements between the new ESO company, and the National Grid Group are described in the next chapter.

Clear and transparent governance arrangements around the new ESO are needed to demonstrate the independence of the new company from other National Grid Group businesses, both in the structure of the ESO Board and its committees, and in the members of the board and their roles.

### Compliance design

#### The ESO Board

NGESO Limited was incorporated in October 2017, company number 11014226. It is separated from the rest of the National Grid Group businesses, performing the electricity system operator role in Great Britain (GB). Please see the corporate structure in Appendix 4 which illustrates this.

The ESO is governed by its own board and various committees to the board. The ESO Board has delegated authority from the National Grid Group Board and has autonomy in decision making on matters in relation to the ESO, in line with its terms of reference.

The ESO Board has eight voting members, including:

- four Non-Executive Directors (NEDs);
- three National Grid Directors and;
- the Chair of the Board, the Director of the Electricity System Operator

As directed by the licence, the seven directors do not sit on any other electricity subsidiary board in National Grid nor on the National Grid Group Board. The profiles of all the ESO Directors can be found at

[www.nationalgrideso.com](http://www.nationalgrideso.com)

<sup>1</sup>Companies Act, 2006, Chapter 2, General Duties of Directors:  
<https://www.legislation.gov.uk/ukpga/2006/46/part/10/chapter/2>

The board directors are duty bound to act in the best interests<sup>1</sup> of the ESO. The NEDs bring independent challenge to ESO decision making and their key responsibilities will include the monitoring of licence compliance and adherence to business separation.

In addition, the ESO has a Compliance Committee and Audit Committee. Both are chaired by a NED and report to the ESO Board on the ESO's compliance performance. The quorum for directors' meetings is three directors, one of whom must also be a Non-Executive Director of the company.

It is intended that the ESO Board will have regular interaction with the regulator through bi-annual meetings to foster a relationship of openness and transparency.

### ESO Governance

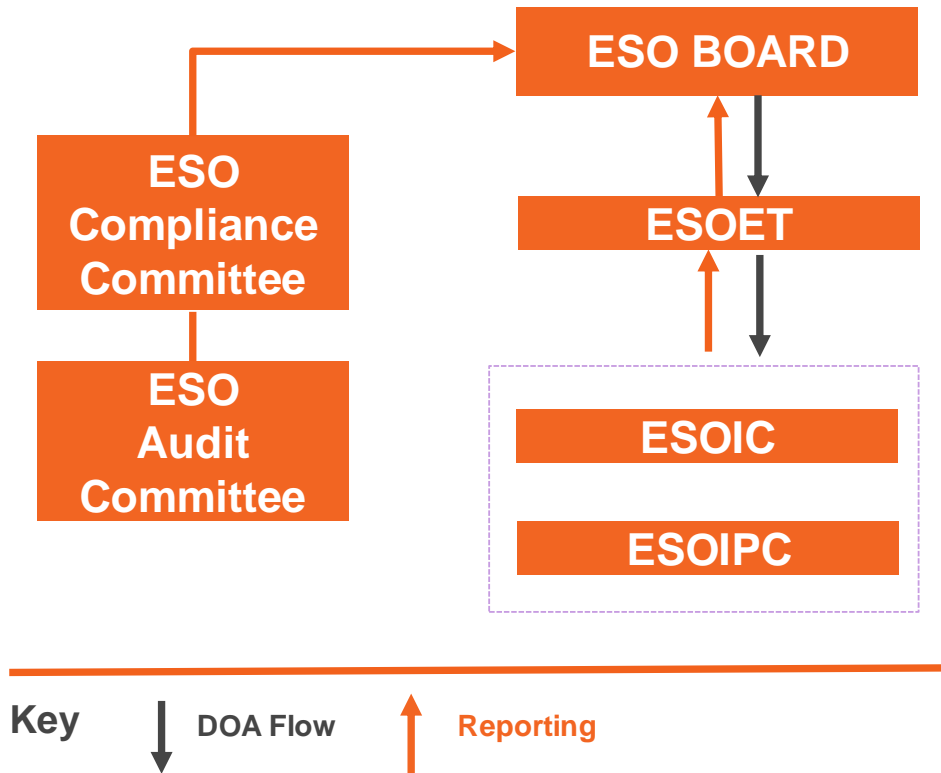
From a governance perspective, the ESO Executive Teams has delegated authority from the ESO Board. The ESO Executive Team is responsible for directing the affairs of the ESO business relating to strategy, markets, operations and financial performance.

ESO Executive Team reports matters into the Board in accordance with the terms of reference and delegations of authority. It is made up of the Director of Electricity System Operator, Head of Strategy and Regulation, Head of Markets, Head of Electricity National Control, Head of Networks, as well as five dedicated business partners for certain shared services (IT, Finance, Corporate Affairs HR and Legal).

ESO Executive Team devolves financial delegation of authority to the SO Investment Committee (SOIC) and Incentives Performance Committee (IPC). SOIC oversees financial decision making, whilst IPC manages the performance of the incentive schemes as well as trading delegations. The attendees for each committee are listed in the table below.

<b>List of attendees</b>	<b>SOIC - ESO</b>	<b>IPC - ESO</b>
Head of Markets	<b>v</b>	<b>v</b>
Head of Business Change	<b>v</b>	
Finance ESO Business Partner	<b>v</b>	<b>v</b>
IT ESO Business Partner	<b>v</b>	
Head of Strategy & Regulation		<b>v</b>
Head of Electricity National Control	<b>v</b>	<b>v</b>
Head of Networks		<b>v</b>

Please see the diagram below which illustrates the ESO governance structure.



All the meeting agendas, minutes and papers are stored on a dedicated and secure data repository and managed by a dedicated technical secretary. All the committee members and technical secretaries have undertaken legal separation e-learning and face-to-face training on the information ringfencing rules. They are the only people who can access the meeting documentation. The meeting agenda, minutes and other documentation will be audited regularly by internal auditors.

# 3. Corporate governance

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# 3. Corporate governance

## 20 Part B and 20.20 (b) (i)

The ESO must ensure it is legally and functionally separate from NGET/NGG/ROCB and confirm the arrangements for managerial and operational separation including arrangements to ensure the independence of the licensee's management board, senior managers and staff from NGET, NGG and ROCB.

## Summary

As a subsidiary of National Grid Group, the ESO needs to interact with the National Grid Group Board. To support operational and managerial separation of the ESO, and independence of the ESO Board, a new Group level committee, the ESO Committee, has been established. The ESO Committee ensures all ESO ringfenced information required to support good corporate governance is viewed separately from other subsidiaries in the National Grid portfolio. The ESO Committee has access to certain ringfenced information required to support good corporate governance and oversight, it is not involved in the day-to-day operation of the ESO. The ESO Executive Team has delegated authority from the ESO Board, to take responsibility for the day-to-day running of the electricity system operator functions. Please see section 5 for more information on this.

The interactions between the ESO Board, the ESO Committee and the National Grid Group Board are visible to the NEDs and the Business Separation Compliance Officer.

## Compliance theme

In addition to the ESO governance structure, demonstrating the independence of governance and decision making in the ESO also comes to life in how the ESO and National Grid Group Boards engage. To enable the ESO to operate sufficiently independently within the National Grid Group, arrangements are needed that allow the shareholder appropriate oversight of the ESO, whilst supporting an appropriate level of independence of the ESO Board. Since legal separation in April 2019, the National Grid Group corporate structure charts (see Annex 4) have been updated to reflect the introduction of two holding companies. These changes do not impact the compliance design or governance of the ESO.

## Compliance design

### ESO and National Grid Group interactions

National Grid Group is responsible for ensuring the long-term viability and prudent financial management of the National Grid Group. As such, being a subsidiary of National Grid Group the ESO is subject to oversight from the Group. The Articles of Association and Matters Reserved to the National Grid Group Board describe the remit of the public limited company (PLC) and are available on the National Grid website.<sup>3</sup> To bring this interaction to life, the areas of ESO activity that have visibility or require approval at Group Board level include things like:

- approval of the ESO's annual budget;
- review and approval of the ESO's three year rolling financial forecast;
- visibility of the ESO's financial performance against its annual business plan;
- visibility of the ESO's principal risks;
- approval of any material extension of the ESO's activities into new business areas or any decision to cease to operate any part of the ESO's business;

<sup>3</sup>Matters reserved for the National Grid Group Board are published on the National Grid website. [Link](#)

- authorisation of changes affecting the capital structure of the ESO;
- approval of the long-term strategic objectives of the ESO and any major changes to the size and composition of the ESO Board and its committees; and
- unforeseen issues that have significant or material impact on the Group (e.g. financial, reputational or principal risks)<sup>4</sup>

### The National Grid Group Executive

The Group Exec is chaired by the CEO of National Grid Group and is concerned with the governance of the Group as a whole (UK/US) and agrees senior staff salaries (excluding Director of ESO). Group Exec ensure that discussions at the Committee comply with the Licences held by NGET; NGG and NGESO. The key tasks cover guiding relations with shareholders and stakeholders (excluding NGESO as this is covered by ESOC), review internal controls and risk management, keep under review and drive improvements in safety and ensure coordination between business units and functions. The Committee also considers reports in relation to matters of ethics and business conduct and compliance matters.

### The UK Executive Committee

The purpose of the Committee is to direct the affairs of the UK Business (excluding ESO) on shared issues including Safety; Cyber Security; Brand & Group Purpose, Vision & Values; Corporate Social Responsibility; National Grid UK Employee Proposition; Talent Management; Union Liaison & Engagement. SOFI is not discussed by the Committee or disclosed in any meeting papers. A separate forum including ESO will operate to consider Talent Management process and policy across the group. The Senior HR Business Partner will provide regular updates to the ESO Board on the talent management process and progress against succession planning for key roles.

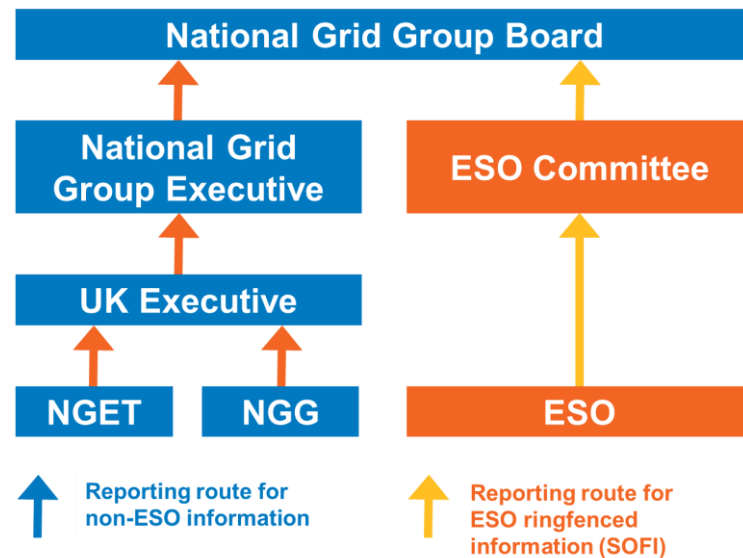
### The ESO Committee

Given the breadth of the National Grid Group, National Grid Group Board prioritises its time and focuses on those matters that are material to the National Grid Group as a whole. It has established several committees to support its work.

To support operational and managerial separation of the ESO, and independence of the ESO Board, a new Group level committee, chaired by the CEO of National Grid Group, the ESO Committee (ESOC), has been established. The purpose of ESOC is to consider and provide oversight in respect of matters relating to the ESO which are to be considered by the Board and/or are matters which would fall within the scope of the authority of the Group Executive. The duties also include guiding ESO in its relations with shareholders / stakeholders, keep under review internal controls, risk management and compliance performance. The ESOC also considers strategic implications that are pertinent to ESO and monitors safety, financial and operational performance and approve certain expenditure and other financial commitments in respect of ESO matters which exceed the authority of the ESO Board. The diagram below illustrates the reporting line between the ESO and National Grid Group. The ESO Committee ensures all ESO ringfenced information required to support good corporate governance is viewed separately from other subsidiaries in the National Grid portfolio.

<sup>4</sup>An example of such a matter is the Hinkley Link Project which was referred by NGET to the National Grid Group Board for approval due to its significant financial and reputational impact. This was notified to the London Stock Exchange and reported in the National Grid Group Annual Report.

in the chapter on information ringfencing.



The ESO Committee is chaired by the CEO of National Grid Group and attended by the Chair of the ESO Board, the Group General Counsel and Company Secretary and the Group Chief Financial Officer. The ESO Committee has delegated authority from the National Grid Group Board with a defined financial delegated authority and its own terms of reference to support the shareholder's interaction with the ESO by reviewing and approving matters within its delegated authority on behalf of the shareholder. The ESO Committee is not involved in the day-to-day operation.

### Governance compliance controls

The Ultimate Controller Undertaking (UCU) is a legally enforceable undertaking in favour of the ESO if the PLC or any affiliate takes action that puts the ESO in breach of its licence. The presence of the UCU drives appropriate compliance behaviours in the PLC and its affiliates, by creating a route of accountability for a licence breach that becomes an integrated part of every National Grid Director's risk and compliance framework. As examples, the presence of the UCU supports:

- i. a focus from the PLC on demonstrating that the corporate governance arrangements do not inappropriately influence ESO decisions;
- ii. engagement from National Grid Group and Corporate functions in diagnostic and remediation activities to prevent misuse of any information that they gain from the ESO through corporate reporting; and
- iii. embedded ways of working in shared services to ensure that ringfenced ESO information is used solely for the purposes of delivering ESO services.

The UCU is reviewed annually, and the Group Board are reappraised of their responsibilities in relation to the UCU, for onward cascade into directorates and teams.

The UCU is one of the Corporate compliance controls providing assurance to the ESO Board on the ongoing commitment to licence compliance from the shared and Group/Corporate functions.

Other controls include:

Appendix 5 provides an overview of the regular reporting cycle and topics covered by the ESO Committee. Information provision to National Grid Group (via the ESO Committee) for corporate governance purposes is described

- Completion of a compliance diagnostic for all Group and Corporate functions that supports corporate governance arrangements for National Grid Group, and implementation of any remediation needed to adhere to the requirements of the new information ringfence and accommodate the ESO Committee;
- Director training – National Grid Board Directors undertake comprehensive training including Director Fiduciary Duties training and are aware of Code of Conduct (Doing the Right Thing) to ensure that they fully understand their obligations;
- Dedicated Group Board Secretariat – the dedicated company secretarial team for National Grid Group follows a structured process for board paper access and submission;
- Document control systems – all National Grid Boards use 'Boardvantage' for end-to-end security for governance and document control;
- Meeting procedures – all Group board meeting agendas and attendees are reviewed and controlled; and
- Audit – the overall governance process is regularly audited by internal and external auditors.

# 4. Financial requirements

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# 4. Financial requirements

## 20.4 and 20.7

The ESO must ensure compliance with Standard Condition B5 (Prohibition of Cross Subsidies), B6 (Restriction on Activity and Financial Ringfencing);

The ESO must ensure its accounts are maintained, and to the extent required by law, audited and reported separately from NGET/NGG/ROCB;

### Summary

To ensure no cross-subsidy between the ESO and any other National Grid Group entities, the ESO has its own, separate accounts. The ESO's statutory accounts will be published in 2020 and subject to external audit.

The ESO has robust debt management and sufficient working capital. The financial structure has resulted in the ESO gaining an investment grade credit rating.

### Compliance theme

The ESO must ensure that certain financial activities are suitably ringfenced from other entities within the National Grid Group. This is to ensure that no cross-subsidies are given to or received from other National Grid entities (Standard Condition B5); that activities are restricted to licensed activities unless specified otherwise in the licence (Standard Condition B6) and that the ESO's accounts are maintained and, where required by law, audited separately from other National Grid subsidiaries (Special Condition 20.7).

The maintenance of separate financial records and accounts is also important to support the informed and independent decision making for the ESO and facilitates efficient and transparent management of allowances.

The ESO also needs to achieve and maintain an investment grade credit rating to be compliant with its licence.

### Compliance design

#### Separate accounts & reporting

The ESO's accounts are maintained and, to the extent required by law, audited and reported separately from National Grid's other subsidiary companies. The accounts provide transparency on separation of the ESO, its costs and revenues.

The ESO will prepare and publish its own statutory accounts in 2020 which will be externally audited.

The ESO will also publish and prepare its own audited Regulatory Accounts in accordance with standard condition B1 (Regulatory Accounts), which also requires a statement describing any costs or revenues charged to or received from the ESO's ultimate controller (National Grid Group) and any subsidiary.

In addition, the ESO maintains separate management accounts on a monthly basis which cover all ESO activities to support the management and decision making of the ESO business and Group oversight.

A full copy of the statutory Report and Accounts and Report of the Auditors for the ESO will be publicly available via Companies House.

The separate financial ledgers described above are appropriately access controlled in line with the ESO's information ringfencing restrictions (see Chapter 6 for further information). These separate ledgers also facilitate the preparation of the ESO financial regulatory reporting pack.

### Prohibition of cross-subsidies

The ESO will ensure that no cross-subsidy is given to or received from any other business of National Grid Group or its affiliates. As mentioned above, maintaining, auditing and reporting separate accounts provides transparency of the ESO's costs and revenues and ensures no cross-subsidies are given or received.

The National Grid Group operates a number of shared services which are available to all Group companies. The way that the costs are apportioned for these services is through the Cost Allocation Methodology (CAM)<sup>5</sup>. There are a number of different factors set out in the methodology as to how the costs are set up (e.g. by headcount, time, volume of service etc.).

These policies are in place to ensure that consistent pricing is applied for services provided to all Group companies.

Specific service arrangements exist between the ESO and NGET covering shared operational systems.

### Restrictions on activity

The ESO does not conduct or carry out any activity other than the transmission business or activities to which the regulator has given its formal consent.

As directed by the Authority on 18<sup>th</sup> December 2018, the ESO has taken over the ownership of ELEXON from NGET, the ownership of ENTSO-E membership and NGET's shareholding in CORESO.

The ESO can carry out de minimis activities as defined in Standard Condition B6 of the licence. Where ESO employees provide a service in this capacity, these activities are outlined in general service agreements (GSAs) and accompanied by internal governance documentation such as standard operating procedures (SOPs) and business procedures.

### Corporate financial structure

The ESO achieved a Baa1 credit rating as a standalone subsidiary of National Grid Group, meeting the requirement for an investment grade rating (see Appendix 12 for a summary of the ratings analysis from Moody's).

An external working capital facility has been established between commercial banks and the ESO; this facility caters for liquidity constraints because of timing issues on payables and receivables. This arrangement, along with the existing debt management process within the ESO and the potential for financial assistance from the National Grid Group, will support the ESO to maintain this credit rating.

<sup>5</sup>The CAM was in place prior to legal separation and already approved by Ofgem.

# 5. Operational separation

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# 5. Operational Separation

## 20.20 (b) (i)

The ESO must demonstrate operational separation from NGET, NGG and ROCB.

### Summary

To enable operational separation of the ESO from the electricity transmission owner (ETO), industry codes were modified using the relevant code governance arrangements. The modifications clarified the responsibilities and accountabilities for operational activities and commercial arrangements between the ESO and ETO, and ESO and other code parties to reflect the new legal entity and align the new relationship with the ETO with other TOs.

To comply with the updated industry regulatory framework, the ESO and ETO have reviewed all their internal business procedures and processes.

Legal separation of the ESO has also strengthened the barriers between and the ESO and NGG and National Grid's non-regulated businesses.

### Compliance theme

Operational separation is the separation of the ESO's licensed activities from those of the other licensed entities (National Grid Electricity Transmission, which continues as the licensee for the ETO, and National Grid Gas, the licensee for the combined gas system operator and gas transmission owner) and National Grid non-regulated businesses (known as Relevant Other Competitive Businesses (ROCB)), like electricity interconnection.

As a single licensed business, the ESO and ETO shared many operational processes and systems. The creation of a separate ESO required a formalisation of these interactions in the electricity industry codes. This codification of the relationship between the ESO and ETO ensures that the ESO's day-to-day interaction with the ETO is transparent and aligned with Scottish TOs and offshore TOs.

Legal separation of the ESO also strengthened the barriers between the ESO and NGG and National Grid Group's non-regulated businesses. These arrangements reinforce the level playing field across all transmission owners and interconnectors and help to address the perception of conflicts of interest within National Grid Group.

### Compliance design

#### ESO and ETO

The following codes were modified to achieve separation of the ESO from the ETO:

- the Connection and Use of System Code (CUSC);
- the System Operator-Transmission Owner Code (STC);
- the Grid Code;
- the Balancing and Settlement Code (BSC);
- the Distribution Connection and Use of System Agreement (DCUSA); and
- the Distribution Code (DCODE).

The types of change to the codes can be categorised as follows.

- (Applying to all codes) Introduction of the new ESO licensee and introduction of “NGESO” as a counterparty (in place of NGET) where relevant;
- (CUSC and STC only) Addressing any transitional requirements to enable the separation. For example, modifications were raised to CUSC and STC to replace relevant code-related agreements from NGET to the ESO; and
- (STC only) Revision of governance arrangements, where required to ensure appropriate panel structures and voting rights to reflect separate NGET and ESO roles.

Most of the code changes aligned ETO arrangements with the Scottish TOs. In a handful of instances (in the Grid Code and STC, in relation to Black Start and voltage control), ETO arrangements are different to those for the Scottish TOs. The need for different arrangements is driven by differences in the technical characteristics and operational complexity of the transmission networks in England and Wales versus the Scottish networks (e.g. different voltage levels, level of network integration and the size of the networks).

The National Electricity Transmission System Security and Quality of Supply Standard (NETS SQSS) was modified to bring it into alignment with the new ESO licence.<sup>6</sup>

To comply with the updated industry regulatory framework, the ESO and ETO reviewed all relevant internal business procedures and processes, making process redesigns in six operational areas:

1. **Managing connections to the transmission network in England and Wales** – In accordance with STC and in line with other TOs, the ETO now enters into a commercial arrangement (TO Connection Offer) with the ESO;
2. **Calculating appropriate Transmission Network Use of System Charges (TNUoS)** – In accordance with the STC, and in line with the activity of the other TOs, the ETO now performs this calculation and passes the information on to the ESO for its calculation of final GB-wide TNUoS tariffs. The ETO can no longer access ESO charging systems and the ETO now produces its own charging statement, which it submits to the ESO to form part of the GB charging statement;
3. **Participation in industry code governance and modifications** – The ESO and ETO are now represented separately on all code panels and each can propose modifications in relation to their respective licensed activities. The ESO retains the role of Code Administrator for CUSC, GC, STC and SQSS, and treats modifications raised by the ETO in the same way as modifications raised by other industry participants;
4. **Contribution to GB transmission network investment planning and coordination** – In line with the responsibilities of the other TOs, the ETO now manages its own network data and provides this information to the ESO as required for the Electricity Ten Year Statement, to create the GB system model and to coordinate transmission investment plans across GB (the Network Options Assessment);<sup>7</sup>
5. **Transmission network outage planning** – In line with the STC, the ESO is no longer involved in the initial development of outage proposals for the ETO. The ESO continues to collate and review proposals from all TOs; and
6. **Operational control** – Accountabilities and responsibilities between the Transmission National Control Centre (TNCC) ‘run by the ETO’ and the Electricity National Control Centre (ENCC) ‘run by the ESO’ are aligned with the requirements of the STC. For example, DNO liaison for system operational activities is managed by the ENCC; and the TNCC needs to agree with the ENCC regarding operational switching for their network.

<sup>6</sup>Full details of all the code modifications raised as part of the legal separation programme can be found on the ESO website

<https://www.nationalgrideso.com/codes>

<sup>7</sup>To note, the Network Options Assessment (NOA) process was already separated within the ESO with enhanced business separation controls between the ESO and ETO. The NOA activities, and the respective roles of the ESO, ETO and other TOs were already in line with the arrangements for operational separation and remain unchanged.



## ESO and ROCB

The ESO and ROCB are operationally separate. The measures to deliver legal separation of the ESO (e.g. creation of the new ESO company, licence and more independent board) reinforce existing barriers between the companies, as does the revision of the Group's corporate governance arrangements to accommodate the new subsidiary (see the 'ESO governance' and 'Corporate governance' chapters for more detail).

# 6. Information ringfencing

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# 6. Information ringfencing

## 20.13, 20.14 and 20.20 (c)

The ESO must ensure that all employees (incl. contractors, consultants etc.) ensure that SOFI is not shared with or used by anyone outside of the ESO other than as per the exceptions in 20.14.

## 20.20 (b) (ii) & 20.20 (c)

The ESO must ensure that systems for recording, processing or storage of data which ESO staff have access to cannot be accessed by NGG, NGET or ROCB employees.

## Summary

Information ringfencing refers to the protection of ESO information (“System Operator Functions Information”, SOFI). It is important that parties should only have access to the SOFI that they need to be able to deliver their licence requirements and fulfil their roles.

To enable the ESO to continue to operate effectively as well as comply with the SOFI protection rules, the ESO has:

- updated its systems and unstructured data with appropriate access controls and restrictions;
- reviewed and redesigned its processes and ways of working; and
- trained its employees on the new information ringfencing obligations.

Exemptions to the information ringfence obligations allow sharing of information between the ESO and other National Grid parties (e.g. the ETO, the shareholder, shared services teams working for the ESO etc) in specific, legitimate circumstances. The ESO and the receiving party have introduced controls to protect SOFI when it is shared through these legitimate routes.

## Compliance theme

The ESO interprets SOFI as all information owned, received or created by the ESO related to its licence activities which is not in the public domain and which could confer an unfair commercial advantage or create a real or perceived conflict of interest if disclosed out of line with one of the legitimate licence exemptions.

As the ESO takes on enhanced roles across the network, such as facilitating a whole system view, facilitating markets and competition, perceptions of conflicts of interest could be generated by others in National Grid Group being able to access the information that the ESO receives and creates. This drives the requirement for the ESO to be able to show that it has appropriately protected SOFI.

Sharing SOFI is often required as part of the ESO’s licence and code-related activities; and is also required to allow National Grid Group an appropriate level of oversight. The ESO also needs to provide transparency on these legitimate channels to share SOFI, to provide assurance that there is no conflict of interest created in the exchange.

Appropriately ringfencing SOFI will also ensure that the ESO does not confer an unfair commercial advantage or engage in discriminatory or preferential treatment to its affiliates in line with the obligations set out in Special Condition 2C.

## Compliance design

### Sources of SOFI

To appropriately ringfence SOFI, sources that contain or potentially contain this information need to be identified. The ESO has two categories of SOFI source: systems and unstructured data.

“Systems” are either operational or non-operational. Operational systems are those which facilitate and carry out ESO licensed activities. Non-operational systems are those that support the functioning of the ESO business, but are not directly related to licensed activity such as its SAP system, or HR data management tools.

“Unstructured data” is a collective term for other places where information and data may be stored or shared. This breaks down to:

- Grey IT – typically operational systems, created and managed locally by teams in the ESO (i.e. not supported by IT shared service);
- Sharepoint sites – for document storage related to specific teams, roles and activities, both operational and non-operational;
- Shared drives – for document storage related to specific teams, roles and activities, both operational and non-operational;
- Distribution lists – that may be used to share SOFI; and
- Mailboxes – email addresses or inboxes.

### Operational systems access control and restrictions

The ESO characterises its operational systems as either:

- **solely owned**/used by the ESO e.g. Market Operation Data Interface System (MODIS), or
- **shared** between the ESO and ETO, NGG or ROCB e.g. integrated Energy Management System (iEMS).

For all ESO operational systems, where they contain SOFI, they are appropriately access controlled.

For solely owned systems, these controls limit access to only those ESO employees requiring access to discharge their roles.

For shared operational systems, they were either ‘soft’ separated or ‘hard’ separated following legal separation of the ESO. Soft separation allows the two businesses to continue to share the same system but introduces new access controls to prevent unauthorised access to the data contained in the shared system. Hard separation is the creation of two separate systems.

For systems shared between ESO and ETO, access controls ensure that SOFI is only disclosed to the ETO as permitted in the licence or the STC. There were a number of shared operational systems where it was not feasible to ringfence SOFI data through access control. In these instances, two separate systems were created, and access controlled as per the “solely owned” systems.

There is only one operational system (enTrader) shared between ESO and NGG (GSO teams only). This has been soft separated.

There are no operational systems shared between the ESO and ROCB.

Maintenance of these access controls is achieved by adherence to the National Grid “Starters, Movers, Leavers” policy. This ensures systematic updating of access controls when employees join the ESO, change role, or leave the ESO.

### Non-operational systems access control and restrictions

Most non-operational systems are shared across many entities within National Grid Group. Where these systems contain SOFI, most are soft separated with appropriate access controls. The ESO has its own, separate SAP system.

Maintenance of these access controls is achieved by adherence to the National Grid “Starters, Movers, Leavers” policy.

### Unstructured data access control and restrictions

SOFI can also be stored and transferred through other means such as shared data repositories, email distribution lists, and mailboxes. The ESO has comprehensive lists of all unstructured data sources owned by each team in the ESO and the shared services teams that support the ESO.

All access lists for the unstructured data sources are up to date and appropriate access controls are in place for every item on the unstructured data lists.

Maintenance of these access controls is achieved by adherence to the National Grid “Starters, Movers, Leavers” policy.

### Reviewing and redesigning ESO processes

The ESO has analysed and carried out assessments of its business processes within the ESO to ensure that any information is shared in a compliant manner with all other parts of the National Grid Group.

### Personal obligations

To ensure its employees and the shared services teams that support it understand the information ringfencing obligations in the licence and any associated process or ways of working changes, the ESO created a training programme on the new requirements. The level of intervention delivered is dependent on the degree to which they handle SOFI.

All impacted employees are obliged to undertake a legal separation e-learning (including a module on information ringfencing). For the introduction of legal separation, this e-learning was completed by ESO and GSO employees, by ETO employees working at the interface with the ESO, by shared services teams that work with the ESO and handle SOFI and by Group and Corporate functions that have access to SOFI through corporate reporting routes.

Teams regularly handling SOFI received face-to-face training on the detail of information ringfencing rules. This was rolled out to all ESO teams, some ETO teams and all shared services teams that support the ESO. The members of ESOC have received face-to-face SOFI training on the detail of the SOFI ringfence rules.

A Code of Conduct for SOFI in Appendix 8 has been developed and implemented across the ESO, articulating SOFI protection principles.

Maintenance of the understanding of personal obligations in relation to the information ringfence is achieved by adherence to the National Grid “Starters, Movers, Leavers” policy. New starters to the ESO, and into the dedicated shared service teams that support the ESO, are obliged to complete the e-learning modules as part of their induction to the business.

## Information ringfencing awareness for third party suppliers and contractors

Anyone working for the ESO is subject to the SOFI ringfencing obligations. This includes external resources such as third-party suppliers of services, contractors, consultants and advisors. Contractors will go through an onboarding process the same as any new starter to the ESO, this includes an e-learning on legal separation, including a module on information ringfencing.

For an agent or advisor through a third party, a training pack has been created to ensure understanding of and compliance with SOFI obligations. The National Grid Supplier Code of Conduct includes obligations to adhere to all business separation requirements including the information ringfence rules.

## How the ESO shares SOFI

The ESO licence sets out the instances when the ESO can legitimately share SOFI. The SOFI disclosure exemptions are listed, along with how the ESO will work within these exemptions to the ringfence requirements:

### **a. When required to by a condition in the ESO licence**

Many activities in the ESO licence require sharing SOFI outside the ESO, e.g. with the transmission owners to support the development of the Network Access Planning documents; sharing SOFI with industry participants such as generators, suppliers, etc. for industry code implementation and development (such as Grid Code, CUSC etc.). The ESO's standard operating procedures and business processes document the basis for this sharing.

### **b. As required or permitted under the STC**

The STC is the code governing the interactions between the ESO and all the transmission owners (the ETO, Scottish TOs, OFTOs and interconnectors) to allow all parties to work together as they undertake their respective licensed activities. The ESO's standard operating procedures and business processes document the basis for this sharing.

### **c. With shared services employees who are performing a role in support of the ESO**

The ESO receives shared services from National Grid Group. Shared services employees can access SOFI to the extent that they need it to provide services to the ESO. All shared services have undertaken a compliance review and have put in place arrangements to ensure ESO information they receive is only used in support of the ESO and is appropriately protected from other National Grid businesses. The chapter on shared services provides detailed description on how they are compliant with the ESO licence, including SOFI ringfencing.

**d. Required by law or regulation, or any governmental or regulatory authority or for the purposes of facilitating the performance of BEIS and Ofgem**

This exemption permits the ESO to share SOFI as required by law or regulation and enables sharing of SOFI between the ESO and governmental and regulatory bodies such as BEIS and Ofgem.

**e. With written consent obtained from the information owner**

The information owner can provide written consent to permit SOFI disclosure by the ESO. Such disclosure needs to be in line with the consent, including the recipient of the information and the purpose of the disclosure. In the instance that a process in the ESO relies on written consent to release SOFI, this consent will be archived alongside the team standard operating procedures and business processes that it refers to.

**f. With NGG for the purpose of emergency management**

As the energy industry becomes more integrated between fuel types, it is important to enable the ESO and the GSO to exchange information to effectively manage emergencies or pending emergencies. The ESO has reviewed and updated the business procedures in relation to crisis management in light of SOFI ringfencing. All instances of its crisis management procedures being invoked are documented; this will include documenting instances where the ESO relied on this ringfence exemption to share information with the GSO.

**g. ESO shareholder access to SOFI to enable effective corporate governance**

As the shareholder of the ESO, the Corporate functions of National Grid Group need access to SOFI to enable effective corporate governance. Corporate governance can be described as:

- effective oversight of the ESO which may require the disclosure of SOFI for e.g. business performance insights, reporting on the ESO's implementation of Group standards and policies etc.,
- shareholder approvals and decision making (as described in the 'Corporate governance' chapter), and
- corporate reporting to enable National Grid Group to fulfil its legal or regulatory reporting requirements.

The ESO shares SOFI with National Grid Group via either the ESO Committee or directly to the National Grid Group Board mainly in the form of regular business reporting. Ad hoc requests from members of the ESO Committee, in line with the matters reserved to the National Grid Group Board, are also permitted. All shareholder requests for SOFI (planned and ad hoc) will be visible to the ESO Board, further detail on information sharing for effective corporate governance is provided in Appendix 5.

**h. Consented by the regulator in written form**

This exemption creates a legitimate route for the ESO to share SOFI outside the scenarios listed in the licence.



# 7. Employee transfer, moves and talent management

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# 7. Employee transfer, moves and talent management

## 20.20 (b) (iv) and 20.20 (b) (v)

The ESO must ensure it has arrangements in place to manage the transfer of employees between the ESO and the Relevant Other Competitive Businesses and the Relevant Regulated Businesses, such arrangements to include treating all such transfers as sensitive and accordingly subject to the review of the compliance officer.

### Summary

Controlling and monitoring the movement of employees<sup>8</sup> ensures that the ESO has the capabilities that it needs, and that all aspects of business separation are appropriately observed when individuals leave the ESO.

ESO employees are contractually aligned to the ESO. Any new starter to the ESO receives an induction and undertakes business separation training to ensure they understand the business, their role and their compliance obligations. Employees moving to any other National Grid entities are subject to the review of the Business Separation Compliance Officer who determines whether special measures are needed to maintain compliance.

The ESO Board has visibility of the process and plan for all ESO Senior Leadership as well as sight of the ESO's strategic workforce planning, diversity and inclusion strategy. The ESO business has autonomy in capability development and recruitment and benefits from access to the National Grid Group's talent pool and talent development opportunities.

### Compliance theme

The ESO's primary resource is its people. To enable the ESO to step up to the new roles and responsibilities, it is important that the ESO demonstrates it can build and develop capabilities in line with the strategic priorities of the ESO business.

Transparency around moves into and out of the ESO business is necessary to dispel perceptions of conflicts of interest that may come from moving ESO talent or expertise to other parts of the Group.

### Compliance design

#### Employee transfers to the ESO

In line with the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE), all employees dedicated to the ESO business were transferred across to the ESO. After April 1st 2019, employees joining the ESO from other National Grid businesses will be moved to the ESO as their contractual employer; anyone leaving the ESO but remaining with National Grid Group will have their contract moved to the relevant company within National Grid Group.

33 employees who are members of the Gas Defined Benefits (DB) Pension scheme couldn't be transferred. The regulatory funding regime does not facilitate the participation of an Electricity licensee in the Gas DB Pension scheme. As such, the ESO is not able to support the pension benefits that relate to the Gas DB Scheme. To retain these people in the ESO, and ensure they are not at a detriment as a result of separation, these individuals will continue to work for the ESO, but their legal employer will remain unchanged.

<sup>8</sup>Employees refer to all staff and managers employed by the ESO.

The cost of these 33 employees is recharged to the ESO to ensure no cross-subsidy. These people will be incentivised based on ESO performance. Any individual that is a member of the Gas DB /pension scheme joining the ESO after April 1st 2019 will also be exempted from the requirement to transfer their contract to the ESO.

As the Gas DB Pension scheme closed several years ago, the ESO is anticipating that, over time, this group of people will reduce. It will provide the updated number of the group in the Annual Compliance Report.

### New starters to the ESO

When joining the ESO, all employees and contractors are given an induction to the National Grid Group, the ESO, the team they will be operating in as well as the role they will be performing.

New ESO staff are provided with an ESO email address. New hires receive new lanyards and passes for identification and access purposes (more detail on this in the 'Physical separation' chapter).

All new starters undergo legal separation compliance training and confirm they understand their compliance obligations. Records of this training are given to the Business Separation Compliance Officer.

### Moving between the ESO and other National Grid businesses

All employee moves from the ESO are subject to review by the Business Separation Compliance Officer. An employee moving out of the ESO needs to complete an offboarding checklist which is subject to individual audit by the Business Separation Compliance Officer.

At the discretion and judgement of the Business Separation Compliance Officer, a cooling-off period may be applied based on an assessment of:

- the employee's access to Systems Operator Functions Information (SOFI) and the commercial and strategic sensitivity of that data;
- the nature and external profile of their current role (e.g. level of interactions with other entities);
- the role they are moving in to (e.g. from a role of dealing with interconnectors into National Grid's interconnector business); and
- the decision making accountability of the employee.

Based on the above assessment, the length of time will be proportionate to the associated risk ranging from 1 month to 6 months. ESO employees with junior roles may be subject to up to 1 months' cooling off period, managers up to 3 months' and the leadership team up to 6 months'. The Business Separation Compliance Officer provides advice as to any special measures which should be applied on a case by case basis and in consideration of specific circumstances and corporate policy.

Other measures for sensitive moves include ensuring that the employee receives an exit briefing to remind them of their obligations under the terms of the ESO licence and their contract of employment. The Business Separation Compliance Officer will also require confirmation that access to systems containing SOFI has been removed.

Upon completion of the exit briefing, the employee signs a declaration to confirm they understand their personal obligations in relation to legal separation. This compliance measure – coupled with the existing data protection obligations in employee contracts – means any negligent breach by an employee could be considered as gross misconduct and result in contract termination.

### Leaving the ESO and leaving National Grid Group

When employees, agents or contractors of the ESO leave the ESO to take up a role outside of National Grid Group, the ESO operates a similar process to internal moves to ensure that these individuals cannot access any systems, data or buildings of National Grid Group once they have left.

The line manager will complete a leaver briefing with the employee involving the completion of a compliance checklist confirming the removal of access to all systems, buildings and other infrastructure.

The Business Separation Compliance Officer will check and validate that the leaver's checklist has been completed properly. This will ensure that these individuals do not have access to any sensitive information, e.g. SOFI, before they leave.

### Recruitment and talent management

The ESO needs the right capabilities to execute the ESO Forward Plan, deliver day-to-day operations and ensure a broader and deeper pipeline of talent for critical ESO roles now and in the future. Effective employee recruitment, development, talent management, retention and succession planning are the routes to achieving this outcome.

The ESO's HR business partner is a member of the ESO Executive Team and conducts regular reviews of short and longer-term capability requirements for the ESO and strategic workforce planning, as well as developing and delivering against diversity and inclusion targets for the current and future workforce. These topics will also be part of regular updates from the ESO's HR business partner to the ESO Board.

In general, all vacancies in the National Grid Group are advertised on the internal jobs board. If internal advertising does not secure a suitable candidate pool, roles will be advertised externally. A sourcing plan is created for each vacancy, and it is at the discretion of the resourcing manager, with advice from the HR shared service business partner, as to the appropriate strategy for each vacancy. In instances where e.g. a new capability is being sought, or specific experience is required that is not readily available within the National Grid Group's workforce, external recruitment campaigns can be triggered immediately.

The ESO is also part of the National Grid Group's talent management process which covers:

- Definition of the talent identification approach and oversight of the execution of this policy to ensure consistency, inclusiveness and robustness of assessments;
- Consideration of future talent demands in relation to the talent pipeline of National Grid Group's employees; and
- Management of succession plans for all Directors and Senior Leadership (Band A and B) and a handful of critical roles in Senior Management and Management (Band C and D).

The ESO leadership team originates talent identification, and succession planning for all levels in the organisation below senior leadership. Except those identified as critical roles, succession planning is managed within the ESO. Succession planning for critical roles and A-B roles are planned as part of the National Grid Group-wide activity ensuring the ESO has access to a deeper pool of candidates. External candidates are also considered as part of the succession planning process.

All those identified as ESO “talent” become part of the National Grid Group process. Their development needs and next steps are originated by the ESO, and will then be discussed at quarterly and annual talent forums led by the HR shared service.

The Group approach ensures that all individuals identified as talent benefit from broadening experiences and career moves that come from being part of a portfolio of related businesses. Being a part of National Grid Group’s talent management process, the ESO leverages the diverse range of roles in the Group to create well-rounded and highly capable leaders with diverse experiences that allow them to take on positions of responsibility in the ESO business.

Talent moves are transparent and fair in relation to movement between entities in the National Grid Group, the requirements of the licence are respected, particularly in relation to operational and managerial separation and independence of the ESO Board.

To demonstrate that the ESO business retains sufficient autonomy in talent development and succession planning and that the National Grid Group does not exert pressure or control over the ESO through the control of talent, the ESO Board will have visibility of the process and plan for all Senior Leadership for the ESO.

# 8. Employee incentivisation, reward and remuneration

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# 8. Employee incentivisation, reward and remuneration

## 20.20 (b) (v)

The ESO must demonstrate arrangements relating to the recruitment and employment of the licensee's employees and the incentivisation of the licensee's managers which, save for managers in dual fuel roles engaged in dual fuel activities, will be linked to the performance of the licensee only.

### Summary

The ESO has made changes to the financial and business measures underpinning how ESO employees are incentivised and rewarded for their performance. The revised measures ensure that ESO employees are only incentivised on ESO performance.

### Compliance theme

Changing measures underpinning the incentives and leading to the reward of staff<sup>10</sup>, managers<sup>11</sup> and senior leaders<sup>12</sup> is a key factor in driving the right cultural shift and behaviours in the ESO that will demonstrate the business is more independent in its thinking, actions and decision making. Aligning individual performance and objectives against those of the ESO, ensures managers and leaders are focused on delivering value to ESO specific activities rather than NGET, NGG or ROCB related activities.

### Compliance design

#### Objectives setting and performance assessment

As a shareholder-owned company, the Board of National Grid Group sets the financial targets and expectations for the ESO for the year ahead considering the Group financial and business plan targets. The ESO will then set its own objectives in line with its own strategy, business plan and priorities. The objectives cascade down across the ESO, from the ESO Board, senior leaders and managers to staff. This ensures that individual objectives are aligned with the targets for and objectives of the business. There are review sessions at each level of the organisation to ensure the objectives are aligned, achievable and challenging. The NEDs will review the Director of the ESO's objectives. All Director's objectives are calibrated on a Group-wide basis, the NEDs will feed into this calibration and have visibility of the outcome.

At the year end, individuals' performance is assessed by their line manager. The Director of System Operator assesses the performance of the ESO Leadership Team and is then assessed by the ESO Committee. There are calibrations across the ESO at each level of the business to ensure that the assessment is fair and a consistent approach is applied. The NEDs will provide performance feedback on the Director of the Electricity System Operator. Director performance is calibrated on a Group-wide basis, the NEDs will feed into this calibration and have visibility of the outcome.

#### Reward and remuneration – Annual Performance Plan

The main components of employee financial reward are base salary and short-term incentive (Annual Performance Plan (APP) / bonus).

<sup>9</sup>For example, there is a UK-wide safety measure for all employees reflecting a Group wide culture of SHE awareness and collaborative positive action

<sup>10</sup>Staff refers to the employees across a broad range of roles from Administration to senior technical / supervisory grades

<sup>11</sup>Managers refers to the employees typically managing teams or functions.

<sup>12</sup>Senior leaders refers to Directors and Heads of Departments



For staff in the ESO, the overall reward framework is subject to collective bargaining with recognised unions. Depending on individual staff performance against objectives, staff will be awarded pay progression and annual bonus accordingly.

For managers in the ESO, increases to annual base salary are recommended by the line manager in line with HR's guidance. The overall budget for the annual managerial salary review is approved by the National Grid Group Executive Committee.

The reward framework for managers and senior leaders is designed to recognise and reward individual performance which consists of two main portions:

- (1) For managers their achievement against business measures, in the form of a scorecard, that links to driving business performance typically in the areas of finance, customer and safety. Senior leaders have financial measures that are related to the scorecard, with a focus on the financial performance of the ESO; and
- (2) All managers and senior leaders have an individual portion to their reward based on 'what' they have achieved against their individual objectives (set at the beginning of the performance year) and 'how' they have achieved it.

The weighting of business versus personal performance changes with seniority, with senior managers and leaders in the business having a larger percentage of their reward based on business performance.

The ESO has re-designed the reward measures underpinning its APP for ESO managers/senior leaders, removing any conflicting measure against the other National Grid asset-related businesses. ESO managers are assessed against the ESO scorecard.

ESO scorecards applying to all ESO managers and staff, and the financial measures used for senior leaders are developed by the ESO Executive Team, based on the approved ESO budget and financial targets for the ESO business. The scorecard measures and financial measures are reviewed and approved by the ESO Board and recommended for onward approval by the ESO Committee.

### Long term performance plan

In addition to the APP, ESO intends to operate a Long Term Performance Plan (LTPP) for ESO senior leaders. There is also scope for including a small number of managers within the LTPP who have demonstrated exceptional performance throughout the year. LTPP awards are made and measured in respect of ESO performance and are in accordance with the Scheme rules and performance measures.

# 9. Visual identity

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# 9. Visual identity

## 20.20 (b) (vi)

The ESO must develop and maintain a new visual and corporate identity for the Licensee's Transmission Business that shall be distinct from those of the Relevant Other Competitive Businesses and the Relevant Regulated Businesses;

### Summary

The ESO has created a new ESO identity and brand to establish a lasting change for the business, its employees, customers and stakeholders. This includes transforming its physical appearance through new logos, imagery and colour palettes and the way its employees present and identify themselves through changing its behaviours and culture.

Its new brand and identity differentiate the ESO from the rest of the National Grid businesses whilst maintaining the brand recognition of National Grid Group as a supportive parent company.

### Compliance theme

The ESO's identity is visualised by a new multi-faceted ESO branding which includes tangible visual elements such as logos, colour palettes and imagery as well as less tangible elements like its culture and behaviours.

The ESO's corporate identity and image are a fundamental part of the way it does business, engages with customers and presents itself externally.

It was important to change the ESO's identity to establish a lasting change for the business. Customers should recognise that the ESO's role and position in the industry is transforming. Being visibly different from the rest of National Grid Group is an important part of helping customers and stakeholders of the ESO understand which part of the National Grid Group they are interacting with, and help to build trust in the creation of a separate, more independent entity.

The culture of the organisation is also changing and the ESO felt that a new identity would help its employees to relate and identify with their new organisation.

### Compliance design

#### What is the ESO's identity?

The ESO has developed a new visual and corporate identity to reflect its growing role in the changing electricity industry.

The new electricity system operator name and logo has been designed as part of a new visual identity that clearly differentiates the ESO from the rest of the National Grid Group. The logo includes the National Grid name to maintain immediate recognition by stakeholders and the wider industry of the continued role the more independent ESO plays, whilst remaining part of the wider National Grid Group. The ESO has ensured that the result is easily distinguishable from other National Grid entities and looks and feels new.

# nationalgridESO

Employees working only for the ESO will always use this identity. As part of the new identity, the ESO will have three new primary colours which are all yellows/oranges. This is distinctly different to the blue of National Grid as illustrated below.

## ESO Primary colours



### Colour



### Typography

Helvetica Neue Light  
**Helvetica Neue Bold**  
Arial Regular  
**Arial Bold**

### Imagery form

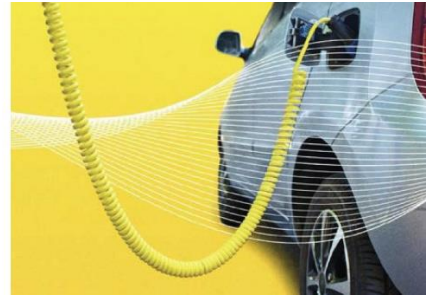


### Illustration



The imagery used throughout the ESO branding has also been updated, moving away from asset-heavy imagery to imagery more analogous with the role that the ESO plays in the UK energy system.

## ESO cut-out imagery



Shared services employees who sit within the dedicated business partner teams will also always use the ESO identity and branding when carrying out their roles. HR will adopt the ESO identity for internal and external recruitment campaigns. Other shared services employees will consider the content of their work when deciding on the correct branding to use (e.g. if it directly relates to the ESO then they will also use this branding).

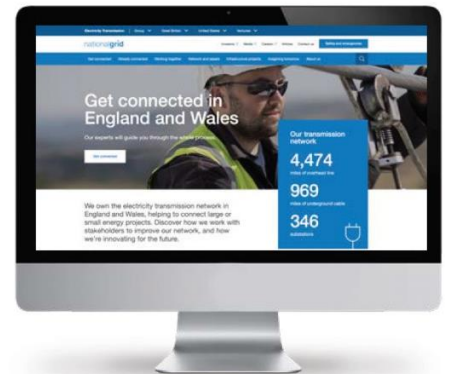
## The ESO's online presence

National Grid Group has created three new websites to help customers find information they require more easily and ensure the ESO has a clearly separate online identity. The three websites are: [nationalgrideso.com](http://nationalgrideso.com), [nationalgridet.com](http://nationalgridet.com) and [nationalgridgas.com](http://nationalgridgas.com).

### ESO website



### ETO website



The Group has also created new social media accounts for the ESO, allowing the ESO to have its own voice on social media. This includes a new ESO Twitter account which will publish milestones such as the launch of a publication or a record being broken, an ESO LinkedIn account which will cover day-to-day topics to do with the ESO and its role, and an ESO YouTube account which plays ESO videos and animations.

### Changing the ESO's culture and behaviours

The new identity is not just about new branding and imagery, it is also about changing the ESO's culture and behaviours. The ESO has trained its employees on how the new identity impacts how they carry out their jobs, how they should speak about their role and the role of the ESO in National Grid Group, and in the sector more generally. This includes ensuring that employees (and the ESO) have a distinct voice in industry, differentiated from other parts of National Grid Group.

Guidelines on how to use the new ESO identity will be maintained and updated on a regular basis. Any employees who are new to the ESO will be subject to the new Starter, Leaver, Mover process which includes detail about the ESO's new brand and how to use it.



# 10. Physical separation

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# 10. Physical separation

## 20.9 and 20.20 (b)(ii)

The ESO must ensure that arrangements are in place which restrict physical access of anyone engaged in the management or operation of ROCB or RRB (excluding dual fuel roles) to any ESO premises occupied by ESO staff or to any equipment, facilities or property employed for the management or operation of ESO.

### Summary

The ESO has changed the physical arrangements for its workspace to help drive the cultural change around legal separation and support other aspects of separation like compliance with the new information ringfence. It has created a new, physically separate office for ESO employees in Warwick called Faraday House.

The ESO has relocated any employees who are directly or solely working for NGG or NGET from its Wokingham site which is the location of the Electricity National Control Centre.

Any National Grid employees outside the ESO or its shared service providers visiting these buildings will be identified and treated the same as an external visitor.

### Compliance theme

Physical separation refers to the buildings that the ESO occupies to carry out its business, and the access rules and restrictions around those buildings.

ESO employees are predominantly based over two locations in Warwick and Wokingham. Prior to separation, the Warwick site was shared between the ESO and the rest of the National Grid Group (excluding ROCB) and the Wokingham site is also home to a small group of corporate shared services.

It is important to create physically separate offices for ESO employees to help drive the culture change around legal separation. Physical separation also underpins and facilitates compliance with the other business separation parameters, such as operational separation and information ringfencing.

### Compliance design

#### Faraday House

The ESO has created a new, physically separate office for ESO employees in Warwick called Faraday House. The full address is: Faraday House, Warwick Technology Park, Gallows Hill, Warwick, CV34 6DA.

Faraday House has a separate entrance to National Grid House with no go-between access for employees. It also has separate facilities for employees, including food and beverage outlets, showers and car parking. This prevents uncontrolled interaction between ESO employees and other National Grid employees. All non-ESO employees visiting Faraday House will be treated as external visitors, with restricted access, and escorted at all times in the ESO working areas.

The ESO has also completely refurbished the interior of Faraday House, implementing the new ESO visual identity throughout the building, including new interior design and signage.

All non-ESO National Grid employees visiting Faraday House will be treated as visitors and therefore subject to visitor policies. All ESO employees now have new identification measures, including new name badges and different colour (orange) lanyards to easily distinguish ESO employees from NGET, NGG or ROCB employees.

Employees in our strategic shared services / business partners and their teams have different lanyards (orange and blue) to allow them to access to both Faraday House and National Grid House. All ESO employees' lanyards are orange only.

### Faraday House reception area



National Grid Group is headquartered at 1-3 Strand in London. ESO employees can continue to access this, albeit guidance has been issued not to conduct meetings with ESO external stakeholders or customers at the Strand. This guidance extends to shared services employees working for the ESO and meeting customers / stakeholders on behalf of the ESO.

### Wokingham

The Wokingham site is the location of the Electricity National Control Centre and is predominantly ESO employees or shared services employees working on ESO projects. There are also some shared services employees working for Corporate Pensions (a transactional shared service) housed on this site.

Any employees based at the Wokingham site who are directly or solely working for NGET or NGG have been relocated.

For the shared services employees based in Wokingham, the ESO has undertaken a risk assessment and applied compliance controls depending on their activity. Any new shared services employees located at Wokingham, or changes to the site, will be subject to the Business Separation Compliance Officer's approval.

# 11. Dual fuel roles and activities

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# 11. Dual fuel roles and activities

## 20.20 (b) (vii)

Provide a description of the dual fuel activities and dual fuel roles.

### Summary

In April 2019 the Electricity System Operator (ESO) was legally separated from the rest of the National Grid UK business. Internally National Grid UK operated a 'one System Operator' model, comprising the ESO and Gas System Operator (GSO). Following a review in December 2019 it became clear that by bringing together the gas system operator and gas transmission business it provided necessary clarity, for our staff and external stakeholders whilst making the legal separation of the ESO even clearer.

### Compliance

Following the review in December 2019 no Dual Fuel roles or Activities exist. ESO remains committed to supporting Whole System thinking as the best approach to future network planning and therefore will continue to publish Whole System publications, though with greater clarity and transparency on the collaboration between National Grid entities.

# 11. Shared services

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# 11. Shared services

## 20.20 (b)(iii)

The ESO must set out the treatment of shared services across the ESO and ROCB and RRB, including a list of the services. Treatment will include – for certain shared services – the provision of a dedicated business partner arrangement to ensure any real or perceived conflict of interests are addressed;

### Summary

National Grid Group operates a shared service model whereby some support functions are shared between the subsidiaries of the National Grid Group. The ESO licence allows this model to continue with some additional rules and restrictions for ESO shared services to comply with.

National Grid Group has reviewed and assessed the processes for all the shared services functions and redesigned processes, changed ways of working, organisational structure, implemented access controls and restrictions within its shared services teams to ensure they can provide support compliant with the ESO licence.

The Group's Finance, Corporate Affairs, Legal, Human Resources (HR) and Information Technology (IT) shared services functions have put in place a dedicated business partner and teams, to deliver the strategic activities which they provide to the ESO. The dedicated business partners are members of the ESOET, they are not ESO employees and their reporting lines are within their respective shared service areas. The dedicated business partners operate with a focused resource and draw upon wider domain expertise and resources (for example HR policy, Group policies). Transactional activities are provided by teams that are shared with other entities in the Group (for example Tax and Treasury).

### Compliance theme

For efficient and effective operation of the business, the ESO benefits from using shared services from the National Grid Group such as Finance, Corporate Affairs, Human Resources, Information Technology, Legal etc. The ESO needs to ensure that the delivery model for these services is appropriate for the nature of the service that is provided; ensuring that services are delivered in a way which respects the requirement of operational and managerial separation and the information ringfence.

### Compliance design

#### The shared service delivery model

The National Grid Group delivery model for shared services has been developed based on the nature of the service provided. These shared service activities are either 'strategic' or 'transactional'. Strategic service activities are those which contribute to direction setting of the ESO business, they are delivered by an individual dedicated to the ESO, under a business partner (BP) arrangement. Transactional activities are back-office, non-strategic in nature and can be delivered by teams working across National Grid Group.

The shared services functions deliver a mix of strategic and transactional activities. Appendix 6 provides a list of the shared service activities that the ESO draws on via its dedicated business partners.

Whilst National Grid Group are continuing to operate with a group-wide shared service model, some services can no longer be provided to the ESO as they are too strategically sensitive to be controlled via a central resourcing model. Because of this, the ESO does not take Regulatory services from a central team, it has its own regulation function, reporting to the Head of ESO Strategy & Regulation.

## Team design, accountabilities and training

The ESO has dedicated business partners for the following shared services: Finance, Corporate Affairs, Human Resources, Information Technology and Legal. The dedicated BPs continue to report to the director of their respective functions, with a dotted line report to the Director of the Electricity System Operator and are members of the ESOET. ESO decision making and business strategy is set by ESOET (see Section 3 on Corporate Governance) and therefore the dedicated BPs are the only people in their shared service function with the authority to contribute to such decisions.

The dedicated BP teams will be treated the same way as ESO employees with respect to the Starters, Movers and Leavers procedures.

All shared services staff (delivering strategic and transactional activities) undertake the shared services legal separation e-learning. In addition, the BPs and their dedicated teams, and some teams delivering non-strategic activity that involves handling SOFI, have face-to-face training on the information ringfence requirements, which is designed for each individual team with bespoke scenarios and examples.

Shared services also use external resources such as consultants, contractors, panel lawyers etc to deliver activities for the ESO. These resources are also subject to the business separation requirements, in the same way that National Grid Group shared services and ESO employees are. All third-party shared service providers are appraised of their obligations in relation to the ESO licence, including information ringfence obligations and the need to flag any potential conflict of interest issues if their organisation is serving multiple entities within National Grid Group.

## Processes and governance

All processes and governance arrangements in the shared services teams that support the ESO (for strategic and non-strategic activities) are documented and have been remediated as needed in line with the ESO licence requirements for information ringfencing and operational and managerial separation.

## Systems and unstructured data

Shared service staff are permitted to access SOFI to support their activities in providing services to the ESO. All systems used by shared services (for strategic and non-strategic activities) have been subject to review as part of the detailed compliance assessment process. National Grid Group has ringfenced SOFI in accordance with the licence obligations in those systems that record, process and store it. This has included validating current access control arrangements and, where required, implementing new or enhanced arrangements to ensure only shared services staff who provide services to the ESO can access the relevant SOFI.

## Control frameworks

National Grid Group has updated licence breach management procedures and rolled them out across all its shared services. Each shared service has a dedicated compliance champion. They are responsible for supporting the function to maintain compliance, including providing guidance and training, advising on compliance remedy actions, and reporting to the ESO Business Separation Compliance Officer to input to the ESO's Compliance Reporting process.

All shared services have provided assurance that all people, processes, systems and data are compliant with the ESO's business separation obligations. On an ongoing basis, this adherence to the compliance framework will be confirmed with the National Grid Group-wide certificate of assurance process.



# 12. Compliance Committee and Business Separation Compliance Officer

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# 12. Compliance Committee and Business Separation Compliance Officer

## 20 Part E

The ESO must appoint a Business Separation Compliance Officer to facilitate ESO compliance with the specified business separation duties.

The ESO must appoint a "Single Appointed Director" to oversee the performance and tasks of the Business Separation Compliance Officer.

The ESO must establish a Compliance Committee to oversee the performance and tasks of the Business Separation Compliance Officer and ensure the ESO is compliant with the business separation requirements of the licence.

## Summary

The ESO has appointed a Compliance Officer to facilitate its business separation compliance. The Compliance Officer is not involved in the management or operation of the system operator functions. They report to the ESO's legal business partner.

A member of the ESO Board has also been appointed as the Single Appointed Director (SAD) to oversee the duties and tasks of the Business Separation Compliance Officer.

A Compliance Committee has been established as a sub-committee of the ESO Board to oversee the ESO's compliance with its business separation obligations. The Committee is chaired by a NED.

## Compliance design

### Business Separation Compliance Officer

The ESO has appointed a competent person to take on the role of the Business Separation Compliance Officer to facilitate ESO compliance with the business separation duties including:

- Standard Condition 20 (Business Separation requirements and compliance obligations and conduct of the System Operator in performing its System Operator Functions);
- Special Condition 2C (Prohibited Activities and Conduct of the Transmission Business);
- Standard Condition B5 (Prohibition of Cross-subsidies);
- Standard Condition B6 (Restriction on Activity and Financial Ring Fencing); and
- Special Condition 2N (EMR Activities)<sup>13</sup>

The Business Separation Compliance Officer is not engaged in the management or operation of the ESO, NGET, NGG or ROCB. The ESO has ensured that the Business Separation Compliance Officer has access to the ESO premises, systems, information, documents and resources required to fulfil their duties and tasks. The detailed description of the duties and tasks of the Business Separation Compliance Officer is listed in Appendix 12.

### Single Appointed Director

In accordance with the ESO licence, a SAD has also been appointed to oversee the performance of the Business Separation Compliance Officer.<sup>14</sup> The SAD is a member of the ESO Board and reports to the board in relation to the obligations set out in Special Condition 20.

<sup>13</sup>The responsibilities of the Compliance Officer for EMR activities are defined in the ESO licence Special Condition 2N.

<sup>14</sup>The profile of the SAD is published on the ESO website.

<https://www.nationalgrideso.com/about-us/meet-ngeso-board>

## Compliance Committee

The ESO has established a Compliance Committee as a sub-committee of the ESO Board for overseeing and ensuring ESO compliance with its specified business separation duties as well as the performance of the Business Separation Compliance Officer.

The Compliance Committee is chaired by a NED and reports to the ESO Board. The Chair of the Compliance Committee certifies whether the annual business separation compliance report fairly represents ESO's compliance with the specified business separation duties.

# Appendices

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# Appendices

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No.	Title	Overview
1	Definitions	Glossary of terms and acronyms
2	ESO Manager Compliance Declaration	Personal declaration of compliance/certification of training completion for all ESO managers and teams
3	Control framework	Summary view of what the long-term control framework will look like. Content and scope currently being finalised
4	National Grid Group corporate structure	Organisational chart showing National Grid Group entities (Updated December 2019)
5	Details of Regular Reporting to the shareholder	Further detail on the annual cycle of reporting that goes to the shareholder
6	List of shared services	List and summary of services provided
7	SOFI Code of Conduct	High level description of SOFI, how employees should share it, protect it and what to do in a breach
8	ESO systems and unstructured data	Overview of ESO systems and unstructured data
9	Business Separation Compliance Officer – role and tasks	Role description of Business Separation Compliance Officer
10	ESO Credit Rating	Moody's Credit Rating summary for NGESO
11	Change Control	Document version history

# 1. Definitions

For the purposes of this statement, unless indicated otherwise, the following definitions from the ESO licence apply:

**“Associate”** means:

- (a) an Affiliate or Related Undertaking of the licensee;
- (b) an Ultimate Controller (as defined in Standard Condition A1 (Definitions and interpretation)) of the licensee;
- (c) a Participating Owner of the licensee; or
- (d) a Common Control Company.

**“Business Separation Compliance Officer”** means the Business Separation Compliance Officer appointed by the ESO in accordance with paragraph 15 of Special Condition 20.

**“De minimis business”** shall have the meaning given in Standard Condition B6.

**“Dual Fuel Activities”** means those activities which are conducted by the ESO in conjunction with National Grid Gas Plc (company number 2006000) (and its successors in title) in its role as gas system operator in order to be delivered in a manner that provides a single combined view of energy security, insights and/or coordination into the interactions between the gas and electricity sectors, and where such activities add value for energy consumers.

**“Dual Fuel Roles”** means those employment positions which are engaged in Dual Fuel Activities and which are specified as such in this compliance statement.

**“Licence”** means the electricity transmission licence granted to the ESO under s6(1)(b) of the Electricity Act 1989.

**“National Grid”** means the National Grid group of companies.

**“NGG”** means National Grid Gas Plc

**“NGESO”** means National Grid Electricity System Operator Limited.

**“NGET”** means National Grid Electricity Transmission Plc.

**“Relevant Other Competitive Business (ROCB)”**

means the business of:

- (a) participating in, or intending to participate in, a competitive tender exercise to determine a person to whom an offshore transmission licence is to be granted;
- (b) an Offshore Transmission Owner;
- (c) undertaking carbon capture and storage activities; or
- (d) owning and/or operating an entity participating in, or intending to participate in, activities which require a licence under section 6(1)(e) of the Electricity Act 1989.

**“Shared Services”** means shared corporate services as specified in Appendix 7 of this compliance statement.

**“Single Appointed Director”** has the meaning given in Special Condition 20.16.

**“Special Condition”** means a special condition of the Licence.

**“Standard Condition”** means a standard condition of the Licence.

**“Systems”** means the IT systems developed to support delivery of the ESO’s business activities and the systems used to store SOFI.

**“System Operator Functions Information (SOFI)”** means all information disclosed to or acquired in any way (and whether directly or indirectly) by the ESO’s employees, agents, contractors and advisers solely by virtue of the performance of system operator functions by the ESO, but excluding all information that is in or has entered the public domain otherwise than as a direct or indirect consequence of any breach of the ESO licence.

# 2. ESO Manager Compliance Declaration

The following text was presented on an online platform as a personal compliance declaration for all ESO leaders and managers to confirm their personal and team readiness for operating in a compliant manner under the ESO licence.

From the 1st April 2019, the ESO will become legally separated within National Grid. To achieve this, we have been designing and implementing changes to our organisation, systems and processes. We also need to change our behaviours and ways of working for the separation to be a success and you are a key element to this.

The purpose for this Personal Compliance Declaration is to confirm that you understand how to continue carrying out your role, compliant with the new rules of legal separation and provide assurance that your team and the processes, systems and data that are part of it are compliant with these new rules:

By agreeing with this declaration, I confirm that:

**I have received and completed the relevant ESO business separation training made available to me:**

- E-Learning (mandatory)
- Classroom training (if applicable)

**To the best of my knowledge, I will be able to carry out my role compliant with the new rules of legal separation and provide the same assurance for my team, by having implemented:**

- Changes to processes or procedures to do with my role and my team
- Changes to access controls to systems and shared areas (e.g. shared drives, SharePoints)
- Changes to ways of working and behaviours (e.g. new team hubs, using new templates)

By clicking the box below, I certify my agreement with this declaration.

I agree

# 3. Control framework

## The ESO knows and understands its business separation obligations

**Compulsory e-learning:** All ESO employees and the shared services teams that work with the ESO on strategic and non-strategic activities understand their business separation obligations through appropriately timed training interventions, including a regular, compulsory refresher of the legal separation e-learning module.

**“My Obligations List”:** All ESO functions own and manage a “My Obligations List”. The list details all legal and regulatory obligations and controls relevant to a team, including business separation obligations. “Mini MOLs” exist at lower levels of management, setting out detailed legal and regulatory requirements for sub-teams, and the control framework in place to manage that obligation. MOLs are updated twice a year, and form the basis of the day-to-day good practice in compliant operation of all teams in the ESO.

**Business separation resources:** The ESO has an intranet site dedicated to providing up-to-date and relevant information on business separation compliance, good practice and training materials. The site is supported by a business separation compliance handbook that provides a summary of employee and team obligations and an easy reference tool into the detailed resources of the intranet site.

**Business separation compliance advice:** The intranet site and handbook are supported by an email “hotline” that employees can use to ask any questions they may have relating to business separation compliance. The hotline is manned by the Business Separation Compliance Officer. The Business Separation Compliance Officer maintains the online knowledge base with Frequently Asked (and answered) Questions from the hotline. The Compliance Officer also works with the ESO and shared services’ network of Compliance Champions (individuals in the ESO teams, responsible for supporting compliant ways of working in local teams), to help them support their teams on all aspects of business separation.

**“Starters, Movers, Leavers” policy:** All employees must adhere to the National Grid Group “Starters, Movers, Leavers” policy. This ensures that new starters are given the appropriate induction training about their business separation obligations.

## The ESO knows its people, what roles they do, and what building access rights they have

**Building access:** The Business Separation Compliance Officer holds a list identifying the building access rights for all employees in the ESO and dedicated shared services team members.

**Moves out of the ESO:** All moves out of the ESO are reviewed by the Business Separation Compliance Officer who makes an assessment as to whether a cooling-off period or other requirement must be fulfilled before the move can be completed.

**“Starters, Movers, Leavers” policy:** All employees must adhere to the National Grid Group’s “Starters, Movers, Leavers” policy. This ensures that the Business Separation Compliance Officer is kept informed about changes and that building access databases are up to date and that the Compliance Officer’s review is triggered whenever an employee leaves the ESO.

## ESO teams know their processes and governance and keep them under review

**Standard operating procedures and business processes:** All teams in the ESO, and the shared services that support them, maintain documentation about the process that they undertake in executing their roles, including documenting processes when they share SOFI in line with licence exemptions. This activity is supported by the SO Assurance Team and their Data Management Library.

**General service agreements (GSA):** The ESO and shared services have GSAs in place that provides a high-level description of the services provided / received. These GSAs are owned by the ESO Executive Team and reviewed annually to ensure that they reflect the service provision and activity and are compliant.

## ESO teams know their systems and unstructured data and keep access lists up to date

**Systems and unstructured data lists:** Each team in the ESO, and each team in the shared services functions that support the ESO, has a comprehensive list of all the systems and unstructured data that they



use. These lists confirm what the system/unstructured data is, whether it contains SOFI, what the access controls are, where the access list is stored and who owns the system/unstructured data.

**General service agreement (GSA):** The ESO and the ETO have a GSA that describes use and maintenance of the systems that they share. The ESO and GSO have a GSA in place that describes the services provided by ESO to GSO. The GSA's are owned by the ESO Executive Team and reviewed and maintained with the ETO.

**“Starters, Movers, Leavers” policy:** All employees must adhere to the National Grid Group “Starters, Movers, Leavers” policy. This ensures that the systems and unstructured data lists owned by each team are kept up to date, and all the access controls are maintained as employee's access is updated in line with individuals leaving the ESO or changing roles.

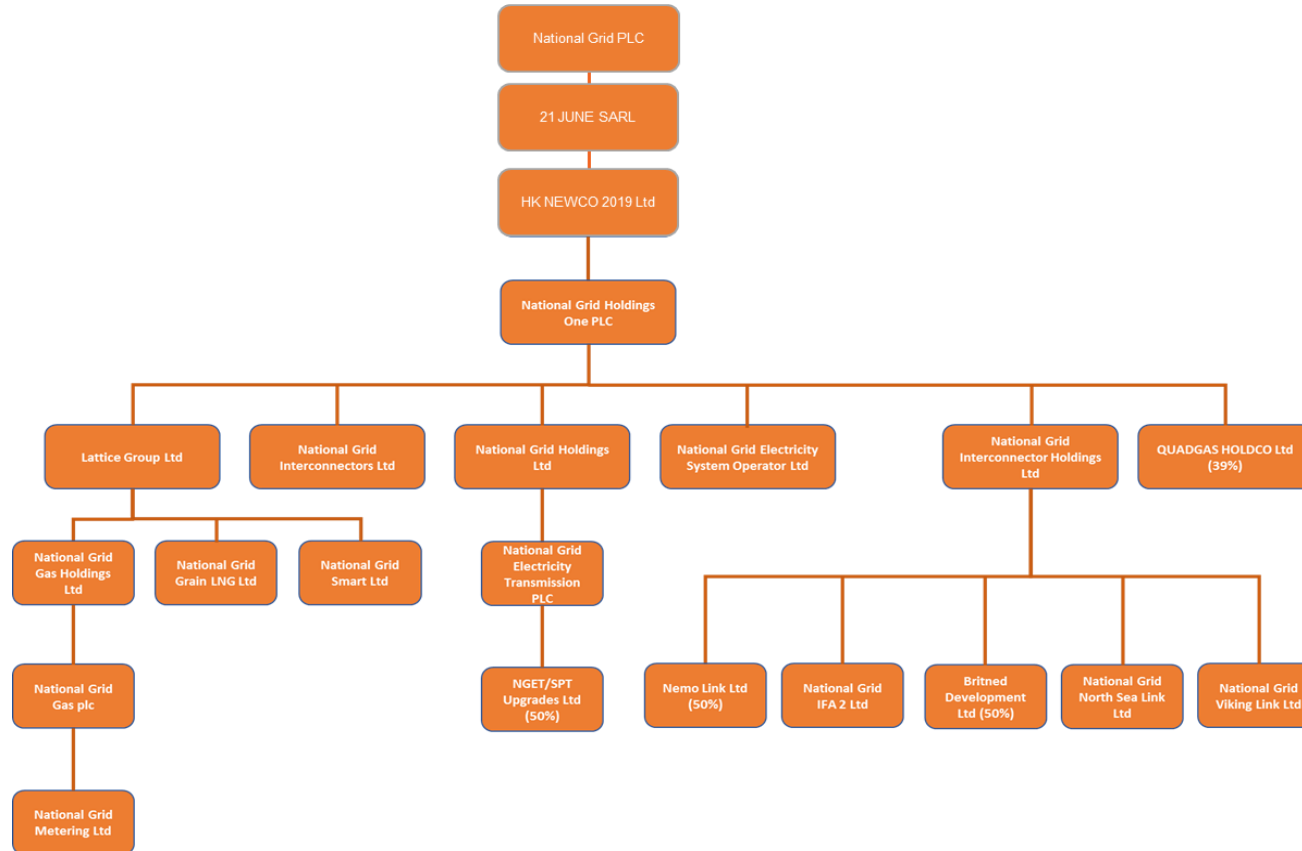
## The ESO follows its governance arrangements and documents inputs and outcomes

**ESO governance:** The ESO Board and its committees, and ESO Executive Team and its committees (SO Investment Committee and Incentives Performance Committee), all have terms of reference. The ESO Board administration is overseen by the ESO Company Secretary. ESO Executive Team administration is handled by the Office of the Director of the Electricity System Operator. Meetings of these governance boards have standing agenda items, and a fixed schedule of meetings. Papers are circulated in advance, minutes are taken and action logs are kept.

**Corporate governance:** The ESO Committee, and other committees that support National Grid Group Corporate Oversight are all supported by the Group Company Secretariat. As for ESO Governance, good practice in terms of meeting administration is observed at all times.

**Corporate ecosystem:** The ESO Board has visibility of all elements of the corporate governance landscape, the forward schedule of activities for consideration by the ESO Board ensures that the ESO Compliance Committee has visibility of all aspects of corporate governance.

# 4. National Grid Group corporate structure



National Grid Group corporate structure (updated December 2019 to include Holding Companies, 21 June SARL and HK NEWCO 2019 Ltd, the changes to corporate structure does not impact the separation or governance of the ESO). This chart was accurate at this date and will only be updated where there are material changes to either ESO or any relevant other National Grid businesses. This chart shows the principal UK operating companies and certain other shareholdings and excludes a number of National Grid subsidiary companies.

# 5. Details of regular reporting to the shareholder

## Shareholder reporting

In accordance with paragraph 20.14 of Special Condition 20, the ESO is permitted to share SOFI with the shareholder to the extent necessary to ensure effective corporate governance. This includes:

- Providing effective corporate oversight of the ESO
- Making decisions on matters that are reserved to the shareholder for approval
- Complying with any reporting requirements prescribed by law, regulations or the rules of any authority.

National Grid Group's corporate governance mechanisms are designed to provide appropriate autonomy of decision making to its operational subsidiaries, including the ESO, whilst also reflecting the requirement for efficient and effective Group corporate governance to ensure the long-term viability and prudent financial management of the National Grid Group.

## How does the ESO share information with the shareholder?

A new Group level committee (the ESO Committee) has been established to facilitate effective corporate governance and oversight of the ESO business. It will report into the National Grid Group Board which will continue to have oversight and approval of the Group as previously described.

## What information does the ESO share?

The information the ESO shares with the shareholder can be categorised in three ways: (1) Regular reporting, (2) Ad hoc reporting, and (3) Approvals.

Annually, the shareholder, via the ESO Committee, will submit a request to access SOFI under the specified exemption, under the three categories outlined above. The ESO Board will send the requested information against the timetable of regular reporting (as outlined below), as and when requested (for ad-hoc requests), and in line with the schedule of standard approvals (as described in the ESO forward meeting schedule, and meeting agendas).

## 1. Regular reporting

The National Grid Group requires all subsidiary companies to report on performance against a defined timetable. This reporting drives accountability for performance throughout the organisation, leveraging planning, reporting and meeting cadence to focus the organisation, creating a standardised approach that supports National Grid Group oversight.

The ESO, in line with the rest of the organisation, follows the defined cadence, which consists of the creation of monthly and quarterly reports and the generation of key performance indicators (KPIs), detailed in the table below:

Report	Contents
<b>Monthly Performance Review (MPR)</b>	<ul style="list-style-type: none"> <li>• This report describes the prior months' actual performance against annual financial targets</li> <li>• Highlights business issues that are impacting performance</li> <li>• Features KPI scorecard: Finance, Operations, Customer, Compliance</li> </ul>
<b>Quarterly Rolling Forecast (QRF)</b>	<ul style="list-style-type: none"> <li>• The QRF is a three-year rolling financial forecast that is updated quarterly to reflect projected performance</li> <li>• Extends the horizon over which National Grid Group plans and takes action on its performance against the business scorecard</li> <li>• Covers: key business priorities; risks and opportunities; KPI scorecard; financial performance; people &amp; hot topics.</li> </ul>
<b>Quarterly Performance Review (QPR)</b>	<ul style="list-style-type: none"> <li>• On a quarterly basis an individual nominated by the ESO Committee will undertake a QPR for the ESO.</li> <li>• Input to meeting includes the latest QRF report, risk and compliance report and deep dive topics.</li> <li>• Deep dive topics cover critical, high impact business issues that require exploration. Topics are identified when the QPR agenda is finalised, based on ESO principal risks, and shareholder risk priorities.</li> </ul>
<b>Quarterly Business Review (QBR)</b>	<ul style="list-style-type: none"> <li>• On a quarterly basis, the Group CEO performs a QBR with the UK, US and NGV business units.</li> <li>• The QBR for ESO is separate from NGG and NGET.</li> <li>• Most notable deep dive issues are tabled.</li> </ul>
<b>Annual Performance Summary</b>	<ul style="list-style-type: none"> <li>• On an annual basis, the ESO will report to the PLC Board on the following:</li> <li>• ESO annual performance</li> <li>• Winter preparedness</li> </ul>

The contents of all reports and the agendas for all meetings are all visible to the ESO Board and summarised as part of the ESO Directors update to the board at every ESO Board meeting. Minutes and actions coming from the regular reporting meetings will also be made available to the ESO Board.

## 2. Ad hoc reporting

The shareholder may from time to time request further information on key performance/issues for corporate oversight purposes. These topics may be released to the shareholder using an established process that records the request, confirms that it comes from a party authorised to request the information (a member of the ESO Committee), records what information was shared, and makes this exchange visible to the ESO Board.

Some examples of topics that may fall under this category are as follows:

- Efficiency saving
- Summer operations
- Winter preparedness
- Digitisation opportunities
- ESO incentives
- Legal separation impact on customers – TO/SO Customer Interactions.

Also, external events / factors that may have an impact on the Group may be requested such as:

- Security of Supply
- Brexit
- Cyber security
- Capacity Market suspension
- Update on open investigations by the regulator or another investigating authority
- Risk management.

### 3. Approvals

National Grid Group determines the strategic direction, business plan, objectives, principal risks and viability of the Group. To ensure effective Group governance, the decision making of all subsidiary companies is subject to National Grid Group for approval or oversight in the following circumstances:

- Where the decision is outside of the subsidiary's Reserved Matters;
- Where a decision is within the subsidiary's Reserved Matters, however, the decision:
  - falls within the shareholder's Reserved Matters in that the decision has a Group impact rather than just a subsidiary level impact;
  - has a resulting financial cost above the subsidiary board's Delegation of Authority (DOA) limit;
  - requires approval due to listing rules e.g. guarantees, or uncapped indemnities with un-excluded indirect/consequential losses (as set out in the DOA policy);
  - is part of a wider Group process and it would be inefficient to be dealt with by the subsidiaries e.g. changes to or escalations required by Group policies or standards.

Matters to be escalated will be shaped and discussed at the subsidiary level before onward recommendation and approval at PLC Board level. Once the approval oversight has been provided, the subsidiary would then carry out the decision e.g. with increased DOA or consistent with the decision

The National Grid Group Board's Reserved Matters are published on the National Grid website:

<https://www.nationalgrid.com/sites/default/files/documents/Matters%20Reserved%20for%20the%20Board%20-%20January%202018.pdf>

# 7. List of shared services

Reference 2O.20(b)(iii)

This appendix provides additional detail on the nature of activities (transactional and strategic) provided to the ESO through the ESO's five dedicated business partners.

- Finance
- Corporate Affairs, including Public & Government Affairs
- Human Resources
- Information Technology
- Legal

The Finance, HR and Corporate Affairs business partners sit on the ESO Executive Team. The IT business partner sits on the ESO Investment Committee. The table below sets out the ESO's shared services:

Function	Service
HR	Trade union meetings
	ER related cases such as Disciplinary, Grievance, Bullying and Harassment, Drugs and Alcohol, Sickness/Absence, Performance
	Oversees and manages ESO contracts of employment
	Oversees and manages ESO recruitment and on-boarding – Employee Referral Reward Scheme
	Oversees and manages ESO recruitment – interview process
	Oversees and manages ESO recruitment reporting
	Oversees and manages ESO recruitment and career development – Employee Moves
	Oversees and manages ESO contractors and agency temps
	Oversees and manages student schemes
	Oversees and manages training course attendance
	Oversees and manages ESO reward – employee incentive schemes
	Oversees and manages ESO reward – appreciate great work (praise and recognition scheme)
Corporate Affairs	ESO communications strategy development
	Employee communications yearly planning
	Public affairs yearly planning

Media support planning

Stakeholder management

Daily news media round-up service

Daily public affairs monitoring

Issue management – ad-hoc/reactive e.g. regulatory investigations, PR issues, press issues etc.

Support for ESO projects (e.g. organisational change)

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Finance –  
Dedicated  
Business  
Partner Team

Business planning for SO

ESO performance management support

Support to ESO strategic decisions including business case assessment and approval, regulatory negotiations, support to ESO impacts of code modifications, investment decision support

Negotiation and agreement of intra-group service contracts

Represents ESO at external forums

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Finance –  
Financial  
Reporting

Provision of technical advice on statutory matters

Preparation of Financial Accounting Returns

Monthly Financial Accounting Close

Management of statutory auditor relationship

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Finance – RIO

Provision of technical advice on regulatory matters

Preparation of Regulatory Returns

Potential representation of ESO and NGET at industry forums or in external regulatory discussions

Financial planning analysis and reporting incl. calc. of specific factors, MOD, RPI

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Finance –  
Control &  
Compliance

Process and controls health assessment

Process and controls redesign

Provision of controls advice

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Finance –  
Planning &  
Analysis

Financial planning process management and oversight

Financial planning incl. consolidation and onward reporting

Monthly management accounts consolidation and onward reporting

Preparation of management reporting incl. UK Exec and Board Papers

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Finance –  
Controllership

Provision of monthly financial accounts and entity financial insight

Preparation of Entity Financial Planning and Narrative

Support to Entity Performance Management

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Group Finance	<p>Audit</p> <p>Pensions</p> <p>Tax</p> <p>Treasury</p> <p>Insurance</p> <p>Investor Relations</p>
IT – Business Relationship Management (BRM)	<p>Overall relationship health including stakeholder management across the ESO, attendance at ESO management meetings and managing escalation of issues</p> <p>Investment planning, including contributing/reviewing investment proposals to support delivery of projects</p> <p>Initiating projects into governance by working with the ESO business and IS teams to develop business drivers, benefits, high level costs, timescales, impact assessments, feasibility assessments, options analysis, resource reqs etc. to support initiation of projects into governance cycles</p> <p>Coordinating innovation into the ESO by working with innovation teams to assess and initiate specific projects as appropriate, e.g. NIC/NIA</p> <p>Identification of new technologies or opportunities to support business capabilities and/or drive efficiencies</p> <p>Development of the RIIO 2 IS Directs business plan with ESO business teams. This includes an overall IS narrative for proposed ESO investments, with individual investment descriptions detailing needs case and benefits.</p> <p>Work with finance to maintain a view on the business plans vs RIIO T1 position</p>
IT – Solution Delivery	<p>Delivery of technical solutions to enable ESO business outcomes. Scope of activity; post-handover from BRM, through design, build, test, deploy. Up to and including transition to Service Delivery.</p>
IT – Infrastructure & Operations	<p>Provides overall management of IS services to the ESO</p> <p>Delivers End User &amp; Collaboration Services to the ESO</p> <p>Provides management of UK Service Delivery Operations</p> <p>Provides Supplier Operational Management</p> <p>Delivers Platform Services to the ESO</p> <p>Global Service Management Centre</p> <p>Provides management and delivery of cloud platforms and hosting centres, data centres and capacity management</p> <p>Delivery of Network Infrastructure Services including telephony systems</p>
IT – Critical National Infrastructure	<p>The UK IS Critical National Infrastructure (CNI) support department provides support and consultation for ESO’s real time (telemetry) &amp; control operational systems.</p> <p>In addition, through direction from our digital risk and security function, CNI manage the cyber protection of the IT estate, working with government departments and IT security consultants, under established policies and using best working practices.</p>



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Regular assessment and reporting to establish compliance is made to CPNI (Centre for the Protection of National Infrastructure).

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IT – Commercial Strategic IS vendor management

- Overall contract performance and adherence to contract obligations
  - Dispute management
  - Work with business teams and Procurement to develop new contract frameworks
  - Supplier market intelligence
  - IS asset management
  - Pricing, chargeback, credit management, spend analysis and value tracking.
- 

IT – Strategy Overall input on major trends and strategic direction for UK IS

- RIIO T2 IS strategy input
  - Overall alignment of ESO CAPEX expenditure with UK capex plan
  - Review of all ESO IS investment papers
  - Alignment of specific ESO business requirements into an aligned IS strategy.
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Legal Provides access to legal advice and support to the ESO from a pool of lawyers and panel law firms across a variety of practice areas including:

Licence/Codes  
Health & Safety  
Litigation  
Corporate Law  
Employment Law  
Disputes

The ESO Compliance Officer provides dedicated services to the ESO, as outlined in the 'Compliance Officer' chapter of this statement.

The ESO Company Secretary provides company secretariat services to the ESO.

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Property Our property function is responsible for:

- Making sure ESO's offices and other properties are in good condition and safe for people to work in
  - Managing the services to run our buildings, such as security, cleaning and catering
  - Providing recycling services and using sustainable materials and energy
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Procurement Support in the negotiation and management of contracts for goods and services  
Provision of expertise to ensure ESO comply with laws on how we buy goods and services

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Other shared services

Corporate functions:  
Treasury  
Tax  
Audit  
Insurance  
Health, Safety & Environment team

# 8. SOFI Code of Conduct

## Purpose and scope

In its role as electricity system operator, National Grid Electricity System Operator Limited (NGESO) will create and receive sensitive, confidential information from third parties which is known as **System Operator Functions Information (SOFI)**.

The ESO interprets SOFI as all information owned, received or created by the ESO related to its licence activities, which is not in the public domain and which could confer an unfair commercial advantage or create a real or perceived conflict of interest if disclosed illegitimately.

The ESO licence Special Condition 20 contains specific obligations which require the implementation of robust practices, procedures and systems to ensure compliance with the business separation duties set out in that condition, including protecting SOFI. Special Condition 20 also contains a specific obligation to establish and maintain a code of conduct governing the disclosure and use of SOFI, which is the purpose of this document.

## Why does the ESO need to protect SOFI?

This code is designed to mitigate the risk of an unfair commercial advantage or conflict of interest arising through the:

- Illegitimate sharing of SOFI with National Grid Electricity Transmission (NGET), National Grid Gas (NGG) and National Grid's non-regulated businesses – like interconnectors and other activities in National Grid Ventures
- Ineffective handling, storage and processing of SOFI
- Use of SOFI for unauthorised purposes.

## Who does the code apply to?

The code applies to anyone engaging with the ESO, including ESO employees, external resources (e.g. agents, contractors and advisers) who are involved in performing system operator functions who require access to, or need to share, SOFI to perform these roles. It also applies to shared services employees who require access to or need to share SOFI to perform their shared services functions in support of the ESO.

All other UK National Grid Group employees should be aware of the code and that they must not seek to obtain an unfair commercial advantage by soliciting SOFI from an ESO employee.

## What are the consequences of breaching this code of conduct?

Failure to comply with this code and the obligations in ESO's licence could result in serious consequences for National Grid Group, including, but not limited to:

- Financial penalties
- Criminal prosecution
- Liability payments to a third party for breach of contract
- Investigations and enforcement action by Ofgem

- Additional and more onerous licence conditions
- Serious reputational damage to the ESO or National Grid Group

An intentional breach of the code by an employee (or failure to report an unintentional breach) will be treated as a disciplinary matter and may result in dismissal. Accidental breach of the code would not generally be viewed as a disciplinary matter, except where the employee has not taken reasonable precautions to comply with this code.

Employees can ask their line manager for guidance in the first instance or contact the ESO Business Separation Compliance Officer for clarification.

### What are the rules I need to comply with?

ESO employees, shared services employees, agents, contractors and advisers

1. **DO** ensure you are aware and comply with document and information system security policies for the secure receipt, storage, classification and sharing of SOFI.
2. **DO** ensure that you are aware of the National Grid Group's Code of Ethical Business Conduct and the terms of this code of conduct for the management and use of SOFI.
3. **DO** ensure you are aware and comply with the Starters, Movers and Leavers policy for employees (including directly employed agents, contractors and advisers) who are joining or leaving the ESO.

1. **DO NOT** make any decisions or actions which are influenced in favour of NGET, NGG or any business that is part of National Grid Ventures.
2. **DO NOT** share SOFI with anyone outside of the ESO unless in accordance with the defined exceptions in Special Condition 20.14 which are:
  - The ESO can share SOFI if it is specifically required to do so as a condition of its licence
  - As required or permitted under the SO/TO Code
  - To shared services employees to the extent necessary to allow them to support the ESO in performing system operator functions
  - The ESO can share SOFI if required by any law or regulation, or any government or regulatory authority has permitted SOFI to be shared
  - The owner of the SOFI data has provided prior written permission for the SOFI data to be shared, so long as the extent to which it is shared is consistent with the scope of the consent
  - To NGG Plc in its role as gas system operator, where NGG Plc requires SOFI data to enable it to perform its role as gas SO
  - To National Grid Group as Ultimate Controller of the ESO, to the extent that the disclosure of SOFI ensures effective corporate governance
  - Where the ESO has received prior written consent from Ofgem to share SOFI.

## All other National Grid employees

**DO NOTIFY** the Ethics & Compliance Manager or Licence Operations Manager immediately if you receive or have access to SOFI and this has not been authorised by the ESO.

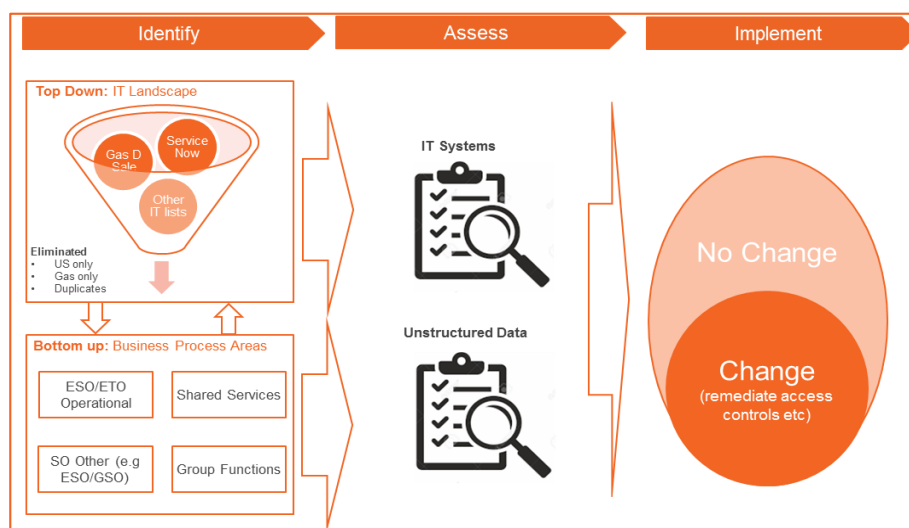
**DO NOT** try to obtain an unfair commercial advantage by encouraging an employee of the ESO or shared services involved in system operator functions to share SOFI.

### What should I do if I discover a breach?

A non-compliance, whether deliberate or unintentional, should be immediately reported to the ESO Compliance Officer via emailing [.box.complianceoffice](mailto:.box.complianceoffice). Immediate steps to contain the incident should also be taken. This could involve actions such as contacting the unintended recipient of the information or recalling the email

# 9. ESO systems and unstructured data

Conceptual approach to identification of ESO systems and unstructured data, assessment against the licence, and implementation of remediation actions:



The table below summarises the total number of systems and unstructured data sources in the ESO and with shared services (that touch the ESO) that have been remediated<sup>15</sup>

Category	Type	ESO	Shared services
<b>Systems</b> (supported by National Grid IT)	Operational	22	-
	Non-operational	5	22
<b>Unstructured data</b>	Grey IT	24	20
	Shared drives	24	28
	Sharepoints	112	41
	Email distribution lists	134	5
	Mailboxes	148	1

Access lists for all systems and unstructured data sources have been reviewed and updated if needed. Numbers in brackets indicate systems that have been remediated either to update access controls and/or to update for other aspects of business separation (visual identity, email address changes etc). Teams in the ESO and shared services that support the ESO hold comprehensive lists of the systems and unstructured data that underpins their work. Adherence to the National Grid “Starters, Movers, Leavers” policy ensures that individual access rights are kept up to date. The presence of the lists allows the Business Separation Compliance Officer to audit compliance on a regular basis.

<sup>15</sup>The total number of system and unstructured data sources that touch the ESO is larger than this. These numbers are just the systems that require changes to access controls to make them compliant with the new arrangements.

# 10. Business Separation Compliance Officer's role and tasks

The role and tasks for the Business Separation Compliance Officer are listed below:

- (a) providing advice and information to the licensee (including individual directors of the licensee) and the Single Appointed Director for the purpose of ensuring the licensee's compliance with the specified business separation duties;
- (b) monitoring the effectiveness of the practices, procedures and systems adopted by the licensee to ensure its compliance with the specified business separation duties and described in the compliance statement;
- (c) advising whether, to the extent that the implementation of such practices, procedures and systems require the co-operation of any other person, they are designed so as reasonably to secure the required co-operation;
- (d) investigating any complaint or representation made available to the Compliance Officer in accordance with paragraph 2O.26;
- (e) recommending and advising upon the remedial action which any such investigation has demonstrated to be necessary or desirable;
- (f) providing relevant advice and information to the licensee (including individual directors of the licensee) and the Compliance Committee established under paragraph 2O.23, for ensuring its implementation of:
  - (i) the practices, procedures and systems adopted in accordance with the compliance statement; and
  - (ii) any remedial action recommended in accordance with sub-paragraph (e);
- (g) reporting to the Compliance Committee any instances which come to their attention, relating to a member of any of the managerial boards of the licensee taking into account the interests of a business other than that in respect of which the board (of which they are a member) has been established; and
- (h) reporting annually to the Compliance Committee as to the Compliance Officer's activities in respect of the specified duties during the period covered by the annual report.

# 11. ESO credit rating analysis

Source, [www.moody.com](http://www.moody.com) (link correct on 1st April 2019):  
[https://www.moody.com/research/Moodys-assigns-Baa1-rating-to-National-Grid-Electricity-System-Operator--PR\\_396553](https://www.moody.com/research/Moodys-assigns-Baa1-rating-to-National-Grid-Electricity-System-Operator--PR_396553)

Rating action:  
Moody's assigns Baa1 rating to National Grid Electricity System Operator  
12 Mar 2019

## First time rating

London, 12 March 2019 -- Moody's Investors Service ("Moody's") has today assigned a Baa1 issuer rating to National Grid Electricity System Operator Ltd (NG ESO), which will operate the electricity transmission system in Great Britain from 1 April 2019. NG ESO, a wholly-owned subsidiary of National Grid Group (National Grid, Baa1 stable) will take over the system operation responsibilities of National Grid Electricity Transmission Plc (NGET, A3 stable) on that date. The outlook is stable.

## RATINGS RATIONALE

The Baa1 rating reflects, as positives, (1) NG ESO's regulation by Ofgem, an experienced regulator with a long track record of transparent decision making; (2) its generally strong energy supplier counterparties, with risk exposure supported by collateral and a regulatory mechanism that should allow for recovery of bad debt under most circumstances; and (3) moderate underlying net debt.

However, the rating is constrained by NG ESO's exposure to potentially material mismatches between the timing of Transmission Network Use of System (TNUoS) payments to transmission owners, around GBP 2.8 billion per year, and the associated recovery from electricity generators and consumers, which may be higher or lower if electricity demand differs from NG ESO's forecast. Although over- and under-recoveries are trued-up through revenue two years later, NG ESO is exposed to the risk of temporary cash outflows that are large relative to its Regulatory Asset Value (RAV) and underlying cash flow. Under-recoveries have historically been as high as GBP 100 million per year, compared to a RAV of around GBP 200 million as of March 2019, and could be higher if British electricity demand fell unexpectedly. NG ESO has mitigated the associated liquidity risks by putting in place a large revolving credit facility that Moody's believes would be sufficient to support several years of plausible under-recoveries and other downside scenarios.

The rating is also constrained by ongoing changes to the regulatory framework, including the proposal that NG ESO should recover a regulated margin on its internal costs from April 2021, rather than a return on its RAV plus regulatory depreciation. Ofgem has not yet provided any guidance on the allowed margin, which will be an important element of long-run returns.

Ofgem's proposal that certain functions of NG ESO could eventually be opened to competition also increases regulatory risk.

In addition, Moody's regards as credit negative the recent introduction of a high-powered incentive/penalty mechanism that will be reliant on subjective assessments of NG ESO's performance. In November 2018, a mid-year review by the independent "performance panel" responsible for this assessment said that NG ESO under-performed on several test areas in the first six months of the 2018-19 regulatory year, the first under the new regime. If the panel does not change its view, Moody's believes NG ESO is likely to incur a penalty for the year.

NG ESO's rating is supported by Moody's assessment that there is a high likelihood that National Grid would provide financial assistance, including increasing its access to liquidity, should it become necessary to maintain NG ESO's credit quality. NG ESO's close integration into the National Grid group is evidenced by use of a common brand, a single treasury function and significant inter-company lending, with all NG ESO's long-term debt provided by National Grid. NGET will be the recipient of two-third of TNUoS payments flowing through NG ESO, and NG ESO will be the source of substantially all of NGET TO's revenues.

### **RATIONALE FOR THE STABLE OUTLOOK**

The stable outlook on NG ESO reflects Moody's expectation that (1) the company will achieve broadly stable underlying cash flows over the remainder of the current regulatory period, which runs until March 2021; and (2) the framework for the forthcoming period (RIIO-2), currently in the consultation process, will not result in materially weaker cash flows or a deterioration in the company's business risk profile. The outlook also reflects the stable outlook on National Grid Plc.

### **WHAT COULD CHANGE THE RATINGS UP/DOWN**

The rating could be upgraded once the regulatory regime for NG ESO has established a longer track record of transparent operation, with NG ESO demonstrating predictable cash flows that provide for adequate and timely cost recovery and a fair return on its investments. The rating could be downgraded if the regulatory framework appeared likely to become less stable and predictable. Any upgrade or downgrade would take into consideration the credit quality of the wider National Grid group.

National Grid ESO operates the electricity system in Great Britain. It is regulated by Ofgem and is ultimately owned by National Grid Plc (Baa1 stable).

The principal methodology used in this rating was Regulated Electric and Gas Utilities published in June 2017. Please see the Rating Methodologies page on [www.moody.com](http://www.moody.com) for a copy of this methodology.

### **REGULATORY DISCLOSURES**

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not



changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on [www.moodys.com](http://www.moodys.com).

For any affected securities or rated entities receiving direct credit support from the primary entity(ies) of this credit rating action, and whose ratings may change as a result of this credit rating action, the associated regulatory disclosures will be those of the guarantor entity. Exceptions to this approach exist for the following disclosures, if applicable to jurisdiction: Ancillary Services, Disclosure to rated entity, Disclosure from rated entity.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Please see [www.moodys.com](http://www.moodys.com) for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

Please see the ratings tab on the issuer/entity page on [www.moodys.com](http://www.moodys.com) for additional regulatory disclosures for each credit rating.

# 12. Change Control

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Version	Date	Author	Change record
1.0	April 2019	Charlotte Ramsay Legal Separation Programme	First submission
1.1	August 2019	Louise Schmitz ESO Regulation	Minor amendments to sections 3, 8 and 11
1.2	January 2020	Louise Schmitz ESO Regulation Steve Rowe Compliance Officer	Addition of full list of shared services  Updated to reflect 1) changes of transitioning Gas System Operator into Gas Transmission, 2) Changes to Group Corporate Structure and 3) updated the number of colleagues in the DB Gas pension scheme
1.3	July 2020	Steve Rowe Compliance Officer	Updated following internal governance review. Included information on; NG Group Executive, Changes to membership of UK Executive and ESO incentive plans

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[nationalgrideso.com](http://nationalgrideso.com)

**nationalgrid**ESO