

# Guidance

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## **(Draft) Conflict Management Audit Terms of Reference**

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The purpose of this document is to establish the Terms of Reference (TOR) for the external audit in Special Condition (SpC) 9.21 Conflict Mitigation Arrangements for Onshore Transmission Tender Exercise.

This document is aimed at Transmission Owners (TOs) who intend to enter an Onshore Transmission Tender Exercise.

This document includes the following:

- Conflict mitigation requirements
- Intentions of the External Audit
- Appointment of External Auditor
- Audit Terms of Reference table

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## **1. Introduction**

### **Conflict Mitigation Requirements**

- 1.1 Transmission Owner's (TOs) can fulfil a dual role in an Onshore Transmission Tender Exercise, both supporting the National Energy System Operator (NESO) in its role as the onshore competition Delivery Body, and by participating as a Bidder in the tender process.
- 1.2 Where TOs participate in an onshore tender exercise, conflict mitigation arrangements are required to ensure that, as a Bidder, TOs receive no unfair advantage through undertaking Tender Support Activities or network planning activities. Any TO that decides to participate in an onshore competitive tender will have to adhere to Ofgem's Conflict Mitigation Methodology.
- 1.3 As part of this requirement, each TO will have to agree a Conflict Mitigation Statement (CMS) with Ofgem prior to the start of the tender process, and then actively manage any potential conflict in line with that CMS. To assess the level of compliance with the approved CMS there is a requirement for TOs to provide an external independent audit report with their Pre-Qualification (PQ) submission and when submitting their tender during the Invitation To Tender (ITT) stage. This document sets out the terms of reference for those audits.

### **Intention of the External Audit**

- 1.4 An external auditor will carry out an audit in line with this document and assessed against the CMS provided by the TO and approved by Ofgem. The audit will assess the level of compliance with the CMS and provide an independent opinion on the degree of compliance with the CMS. The audit report will include:
  - Scope, audit objectives, and audit methodology
  - Findings, evidence to support findings, and impact of findings.
  - Conclusions, recommendations, and actionable suggestions
- 1.5 The auditor will rank conclusions in terms of a RAG classification reflecting the degree of compliance as follows:

- **RED:** The TO has not complied with its CMS in one or more of the key areas of the CMS in a manner that is likely to have provided an unfair advantage in preparing its tender.
- **AMBER :** The TO has not complied with its CMS in one or more of the key areas of the CMS but in a manner that is unlikely to have provided an unfair advantage in preparing its tenders.
- **GREEN:** The TO has complied with its CMS in all material respects.

1.6 Should the external audit identify any Red or Amber classifications, the TO will be given an opportunity to rectify any issues ahead of commencement of on Onshore Transmission Tender Exercise. If, following efforts to rectify any issues, the RAG rating is still Red then the TO will not be permitted to enter as a Bidder. If the RAG rating is Amber, Ofgem will consider whether the non-compliance gives rise to any unfair advantage to the TO and will consider whether the TO is permitted to enter as a Bidder on a case-by-case basis.

1.7 The audit will address key areas of the CMS, including sub-sets defined in the audit framework outlined in the next section:

1. Separation of the licensee and the bidding unit
2. Employee Transfer Restrictions
3. Managerial Separation
4. Information Sharing Restrictions
5. Financial Separation
6. Monitoring & Reporting Compliance

### **Appointment of External Auditor**

1.8 Given the significance of the role of the external auditor in the process set out above and the reliance that will be placed on the opinion of the auditor, Ofgem may wish to place requirements on the TOs participating as a Bidder in relation to the credentials, selection process and terms of engagement of the auditor.

1.9 Ofgem will consider specifying minimum requirements for the credentials and qualifications of the external auditor to ensure the party selected has demonstrable independence and the required level of expertise. Ofgem require

any external auditor to be accredited by the Royal Institution of Chartered Surveyors (RICS).

- 1.10 Whilst it is the TO's responsibility to appoint the auditor, Ofgem may require to be involved at some level in the procurement process. The level of involvement could range from a simple right of veto over the name put forward by the TO to a more active role including input into the evaluation criteria for a competitive procurement process.
- 1.11 Ofgem must give written approval of the auditor to the TO before undertaking the external audit, and any reports from the external auditor relating to the compliance audit, including interim reports, must be provided to both the TO and to Ofgem.

## 2. Scope of Work

| Area                | Sub-area                 | Audit objectives   | Audit criteria   | Evidence gathering methods   | Expected findings  | Audit Rating | Potential messages/conclusions |
|---------------------|--------------------------|--|--|--|--|--------------|--------------------------------|
| Business Separation | Organisational structure | Ensure there is clear organisational separation between the bidding unit and the element of the TOs organisation that is supporting the CSNP and tender process except persons engaged in the provisions of shared services. | <ul style="list-style-type: none"> <li>• Explanation of organisation structure</li> <li>• Signed declaration of interests that identify potential conflicts.</li> <li>• Identification of when the business unit was separated.</li> <li>• Responsible board member identified.</li> <li>• Board member has clear understanding of their responsibility in relation to potential conflicts.</li> </ul> | <ul style="list-style-type: none"> <li>• 1 to 1 interview</li> <li>• Conflicts management register</li> <li>• Declaration of potential conflicts</li> <li>• Organisational diagram that shows clear separation</li> <li>• Business communication showing business separation and when it went live.</li> </ul> | <ul style="list-style-type: none"> <li>• Conflicts management register is up to date and aligned to declarations.</li> <li>• Clear separation of business units</li> </ul> |              |                                |
| Business Separation | Ongoing compliance       | Ensure there is a robust communication of any changes  | <ul style="list-style-type: none"> <li>• Ensure robust change process is in place.</li> <li>• Confirm Ofgem have been informed of any changes.</li> </ul>  | <ul style="list-style-type: none"> <li>• 1 to 1 interviews (Ofgem and TO)</li> <li>• Updates to organisation structure</li> </ul>  | <ul style="list-style-type: none"> <li>• Changes to the organisation have been formalised.</li> <li>• Any changes to the key decision have</li> </ul>                      |              |                                |

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| Area                           | Sub-area | Audit objectives  | Audit criteria   | Evidence gathering methods  | Expected findings   | Audit Rating | Potential messages/conclusions |
|--------------------------------|----------|---|--|---|---|--------------|--------------------------------|
|                                |          |   | <ul style="list-style-type: none"> <li>Changes have been ratified by key decision maker</li> </ul>   | <ul style="list-style-type: none"> <li>Formal communication of change</li> </ul>  | <ul style="list-style-type: none"> <li>been communicated.</li> <li>Demobilisation stakeholder management plan in place</li> </ul> |              |                                |
| Employee Transfer Restrictions | Process  | Confirm that the Bidding Unit has processes and procedures in place that will not utilise the services of any employees of the TO who are involved in a project's initial design or undertaking Tender Support Activities | <ul style="list-style-type: none"> <li>Understand the process that defines the timing and nature of employee separation.</li> <li>Organisation charts showing which employees are in each business unit.</li> <li>Change control process is in place for the transfer of employees.</li> <li>Defined approval process in place to govern employee transferred clearly linked to CMS</li> </ul> | <ul style="list-style-type: none"> <li>Conflicts management register is up to date.</li> <li>Records of employee transfer and approvals</li> <li>1 to 1 process walk throughs that demonstrate all involved in process understand it</li> </ul> | <ul style="list-style-type: none"> <li>Robust processes in place to control employee transfers</li> </ul>                         |              |                                |
| Management separation          | Set up   | To ensure there are discrete management   | <ul style="list-style-type: none"> <li>Management separation exists up to but not including</li> </ul>   | <ul style="list-style-type: none"> <li>Presentation and organisational diagrams</li> <li>1 to 1 interview</li> </ul>  | <ul style="list-style-type: none"> <li>A clear diagrammatic representation and explanatory</li> </ul>                             |              |                                |



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|                       |                    | structures for the bidding unit  | <p>the TO Parent Board.</p> <ul style="list-style-type: none"> <li>• Check that confidentiality agreements are in place</li> </ul>           | <ul style="list-style-type: none"> <li>• Review of confidentiality agreements</li> <li>• Change control procedure for management movements and changes</li> </ul>   | <p>text showing how the management structures of the TO and the bidding unit are entirely separate up to the TO Parent Board</p> <ul style="list-style-type: none"> <li>• Confidentiality agreements in place between different management structures</li> </ul> <p>Control of management movement between different structures</p> |              |                                |
| Management separation | Ongoing compliance | To assess whether there is ongoing management of conflicts and potential conflicts | <ul style="list-style-type: none"> <li>• Check the robustness of the overall and ongoing arrangements for management of conflicts</li> </ul> | <ul style="list-style-type: none"> <li>• Frequency of regular reviews of the conflicts register.</li> <li>• Communication protocols in place for informing Ofgem of any changes and examples presented</li> </ul> | <ul style="list-style-type: none"> <li>• Monthly review of conflicts as a minimum</li> <li>• Evidence that TO has informed Ofgem if changes have occurred.</li> <li>• Ofgem informed of a new potential conflict within 5 business days.</li> </ul>   |              |                                |

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| Area                             | Sub-area                      | Audit objectives   | Audit criteria  | Evidence gathering methods   | Expected findings   | Audit Rating | Potential messages/conclusions |
|----------------------------------|-------------------------------|--|---|--|---|--------------|--------------------------------|
| Information sharing restrictions | Set up                        | To assess whether TOs are treating information related to tender support activities confidentially | <ul style="list-style-type: none"> <li>Assess the appropriateness of confidentiality agreements between TOs, Delivery Body and Bidders.</li> </ul>  | <ul style="list-style-type: none"> <li>Confidentiality or Non-Disclosure Agreements in place and signed by impacted staff</li> </ul>   | <ul style="list-style-type: none"> <li>Confidentiality is understood and necessary processes and procedures are in place to support this</li> </ul>   |              |                                |
| Information sharing restrictions | Set up and ongoing compliance | To confirm that digital barriers and the controls around such are robust                           | <ul style="list-style-type: none"> <li>Assess the digital barriers and ethical wall to ensure that they provide real separation of digital data and information is managed effectively within this environment</li> </ul> | <ul style="list-style-type: none"> <li>A description of the digital environment and how the digital environment is separated.</li> <li>A document showing who is the data and access controller.</li> <li>The process for requesting, accepting and approving access to different environments.</li> <li>A check list to ensure that the data access controller understands when a person cannot have access due to their role or a</li> </ul> | <ul style="list-style-type: none"> <li>Well defined and well separated digital data environment.</li> <li>A well established and well-known data access and control process is in place supported by training.</li> <li>Confidence that any data breaches will be notified and managed effectively</li> </ul> |              |                                |

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|   |                               |   |  | <p>potential conflict.</p> <ul style="list-style-type: none"> <li>• Training material and a training matrix showing people involved in the competition have understood the new data environments and access control requirements</li> </ul>              |  |              |                                |
| Financial separation                                      | Set up and ongoing compliance | To confirm that the TO and its bidding unit are financially separated                   | <ul style="list-style-type: none"> <li>• Find that the business units are financially separated and in line with current license agreements</li> </ul> | <ul style="list-style-type: none"> <li>• Records of profit and loss accounts is applicable.</li> <li>• Examination of financial payment applications</li> <li>• List of people within each business units</li> <li>• Monthly business reports</li> </ul> | <ul style="list-style-type: none"> <li>• No cross billing or recovery of costs of the bidding unit are not recovered by other areas of the business</li> </ul> |              |                                |
| Monitoring, reporting and ongoing management of Conflicts | Set up                        | To assess whether that the TO is reporting compliance against its CMS fully and fairly. | <ul style="list-style-type: none"> <li>• To examine and decide how effectively the TO is reporting compliance</li> </ul>                               | <ul style="list-style-type: none"> <li>• Overall CMS process</li> <li>• Communication of the appointment of the Conflicts Management Officer (CMO)</li> </ul>  | <ul style="list-style-type: none"> <li>• High degree of compliance with all parts of the CMS</li> <li>• Strong management processes in place to</li> </ul>     |              |                                |

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|      |          |                  |                | <ul style="list-style-type: none"> <li>• Terms of reference for the CMO showing the interdependence of the CMO</li> <li>• Acceptance and understanding the CMO role.</li> <li>• Conflicts Register</li> <li>• Declarations of Interest</li> </ul> | <p>support the CMS.</p> <ul style="list-style-type: none"> <li>• High degree of reporting is readily available.</li> <li>• There is an ongoing process in place for the management of conflicts</li> </ul> |              |                                |

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