



Energy for
generations

ESB Generation and Trading's
Response to Compensation
Arrangements for Net Transfer
Capacity Reductions Consultation
(SEM-23-024)

05/05/2023



1. INTRODUCTION

ESB Generation and Trading (GT) welcomes the opportunity to respond to the Compensation Arrangements for Net Transfer Capacity Reductions Consultation Paper (SEM-23-024). The consultation sets out:

- the existing arrangements under the Interim Cross-Zonal Arrangements (ICZAs);
- detail of the methodology adopted in 2021 in Great Britain; and
- outline of the EU regulatory framework, including an overview of how cross-zonal capacity is calculated, provisions concerning NTC reductions and references to compensation.

The paper also includes details on the capacity calculation methodologies developed by the Ireland-UK (IU) TSOs and approved by the IU RAs as well as a reference to the Trade and Cooperation Agreement (TCA), which provides for the development of electricity trading arrangements between the EU and UK.

We understand that the purpose of this consultation is to encourage industry and stakeholders to share their views on the arrangements going forward in the SEM. We support this stakeholder engagement approach and recognise that in the interim period, ahead of the implementation of Multi Regional Loose Volume Coupling (MRLVC), a methodology needs to be agreed in relation to the compensation arrangements in the SEM for reductions in Net Transfer Capacity (NTC) on SEM-GB interconnectors. We trust you will find our comments both helpful and constructive.

2. EXECUTIVE SUMMARY

ESB GT acknowledges that in this interim period post-Brexit and ahead of the introduction of MRLVC, the interim ICZAs will continue to apply to the Greenlink Interconnector and any future SEM-GB interconnectors, with the exception of Article 3 (20, 21 and 22), which relates to the compensation arrangements in the case of a reduction in net transfer capacity (NTC).

We also recognise that the provisions outlined in Article 3 were conceived in the context of Financial Transmission Rights (FTRs) being sold on the SEM-GB interconnectors. Post-Brexit, interconnector owners can no longer earn the revenue from FTR auction receipts, therefore the underlying logic that was used for development of those provisions is no longer in line with current market arrangements.

ESB GT understands that the rules need to provide a clear explanation about how interconnector owners will be compensated during periods of NTC reduction, and we are therefore support the RAs

intention to clarify the methodology that will be applied going forward. However, we also recognise that that this should only happen in the rarest occasions to ensure system security.

We consider that the existing arrangements in GB¹ cited in the consultation paper (Section 2.2), seem appropriate for SEM-GB interconnection, and therefore have the potential to provide an effective means of clarifying the NTC reduction compensation arrangements for market participants. We also support the adoption of the existing ICZAs principles of 'causer-pays' and 'cost neutrality' and the inclusion of the principle that there will be 'different compensation arrangements for allocated and unallocated capacity'.

ESB GT emphasises the need for any revised arrangements to be assessed against the wider market arrangements to mitigate any potential impact or unintended consequences on other market participants, in addition it should not give rise to any perverse incentives for the interconnector owners. In addition, we are in favour of the use of common NTC reduction compensation arrangements across all SEM-GB interconnectors. ESB GT supports the need to further optimise the TSO's obligations in terms of demonstrating or codifying the underlying conditions that will give rise to an NTC reduction being declared and would expect there to be transparent reporting were such events to arise.

ESB GT understands that the Trade and Cooperation Agreement (TCA) between the UK and the EU outlines a new procedure, Multi Regional Loose Volume Coupling (MRLVC), which is designed to provide an enduring solution for the allocation of interconnector capacity at the day-ahead time frame. We support the timely introduction of this new procedure which we will unify the approach to capacity calculation for the EU-GB cross-border allocation.

We also draw attention to the SEMC's request to have an additional assessment carried out by interconnector owners for the implementation of Physical Transmission Rights (PTRs) ahead MRLVC implementation in SEM-GB Cross Border Trading (SEM-23-012)², as we consider that the outcomes of this assessment are expected to have an impact on any revised NTC reduction arrangements.

Finally, we emphasise the need for the revised arrangements to take into consideration compatibility with the methodologies used within the EU for Cross Zonal NTC reductions (as well as GB) to ensure level playing field for all interconnectors on the island of Ireland. This is especially important since the Celtic interconnector may commence operation ahead of MVLRC as the revised timing for the introduction of this mechanism remains uncertain.

¹ [download \(nationalgrideso.com\)](https://nationalgrideso.com)

² [GB-SEM Trading Decision Paper .pdf \(semcommittee.com\)](#)

3. QUESTIONS

- 3.1 Please set out your view on the appropriate arrangements for NTC reduction compensation going forward in the SEM, given the current arrangements for cross-border trading. Would this be impacted if cross-border forward hedging instruments were introduced in advance of MRLVC and, if so, in what way?

In relation to the use of the NTC reduction measure, ESB GT draws attention to the fact that it is considered the last resort measure³ in solving any distortion between supply and demand on the island of Ireland when other market-based options are exhausted. We therefore remark on the fact, also noted by the RAs in the consultation, *that the SEM TSOs have curtailed transfers, both partially and fully, across the existing SEM-GB interconnectors (Moyle and EWIC) on a frequent basis since September 2021.*

ESB GT supports the use of common NTC reduction compensation arrangements across all SEM-GB interconnectors (not only Greenlink) as well as any future SEM-GB interconnectors. In our view a common mechanism which covers the range of scenarios that can be expected to arise, will reduce complexity and create transparency for all market participants. In addition, this approach is also expected to minimise the possibility of future disputes due to different methodologies being applied to different interconnector owners. In our view the existing arrangements in GB cited in the consultation paper (Section 2.2), seem appropriate for SEM-GB interconnection, and therefore have the potential to provide an effective means of clarifying the NTC reduction compensation arrangements for SEM market participants.

ESB GT emphasises the need for the revised arrangements to be assessed in line with the wider market arrangements to mitigate against the potential impact of unintended consequences on other market participants. ESB GT supports the need to further optimise the TSO's obligations in terms of demonstrating or codifying the underlying conditions that will give rise to an NTC reduction being declared and would expect there to be transparent reporting were such events to arise. Indeed, we stress the need for transparency in the market and the importance of informing market participants of the overall costs of the NTC reduction measure, as it is a non-energy action taken by the TSO outside of the regular market arrangements.

³ [EirGrid-and-SONI-Balancing-Market-Principles-Statement-V6.0.pdf \(eirgridgroup.com\)](#) part 3.4.6. Prices and Volumes for Cross-zonal Actions, Emergency Instruction -EI

Finally, we draw attention to the fact that there is currently no firm decision from SEMC on the introduction of long-term hedging instruments in advance of MRLVC. Therefore, in view of the delays in publishing the updated timeline for the introduction of MRLVC, we consider that it would be appropriate for any revisions to the ICZAs to have the ability to accommodate the potential introduction of cross-border forward hedging instruments in the future.

ESB GT supports the use of common NTC reduction compensation arrangements across all SEM-GB interconnectors. We also emphasise the need for the new arrangements to be assessed in line with the wider market arrangements to mitigate against the potential impact of unintended consequences on other market participants both now and in the case where cross-border hedging instruments were to be introduced in the future.

3.2 This paper references various principles that underpin different approaches to compensation arrangements for NTC reduction (i.e. ‘causer pays’, ‘cost neutrality’, ‘different compensation arrangements for allocated and unallocated capacity’). In your view, what principles should underpin compensation arrangements for NTC reduction going forward in the SEM?

ESB GT notes and support the following principles currently included in the ICZAs:

- Article 3(19) – is based on ‘causer-pays’ principle and states: *that once the causer of a reduction in NTC is determined ex-post, the Interconnector Owner /Administrator shall invoice the causer for reimbursement.*
- Article 3(20) – is based in the ‘cost neutrality principle’ and sets out the compensation methodologies for different timelines via the use of loss adjusted market spreads.

ESB GT supports the adoption of both principles when considering any revisions to the ICZAs. In addition, we support the introduction of ‘**different compensation arrangements for allocated and unallocated capacity**’ in any revised arrangements to avoid creating perverse incentives for interconnector owners. In our view the inclusion of this principle will ensure that all scenarios are appropriately covered and will therefore enable the overall payment of any NCT reduction to be determined correctly.

Revised arrangements should adopt the existing ICZAs principles of ‘causer-pays’ and ‘cost neutrality’ and also include the principle ‘different compensation arrangements for allocated and unallocated capacity’.

3.3 Are there any other factors, not covered in this paper, which should be considered by the RAs ahead of a decision? If providing, please explain relevance.

As set out in the SEM-GB Cross Border Trading Decision paper additional assessment carried out by interconnector owners for the implementation of PTRs has been requested by SEM Committee. ESB GT shares the view that the final decision about revised arrangements regarding NTC reduction should be taken in conjunction with the findings of this assessment.

In addition to the above, the timeline of MRLVC implementation directly affects the period for which these revised arrangements will be applicable. If the MRLVC solution is not delivered in time for the Celtic Interconnector start of operation the revised SEM-GB arrangements should be compatible to methodologies used within the EU for Cross Zonal NTC reductions to ensure level playing field for all interconnectors on the island of Ireland.

ESB GT suggests that both PTR implementation assessment carried by interconnector owners and the impact of implementation timeline for MRLVC are taken into consideration when developing the revised compensation arrangements.

4. CONCLUSION

ESB GT recognises the need for an interim solution ahead of the MRLVC to ensure that investors in interconnectors are not adversely affected when NTC reduction events are called by the TSOs. We also agree that the principles that have been adopted in the ICZAs should remain in place.

In addition to providing the relevant compensation for allocated or unallocated capacity across interconnectors we also believe that this should be a universal methodology applicable all current and future interconnectors. This will ensure that there is stability in the market and that this is not just a short run remedy.

Finally, in our opinion it is important to have effective transparency not only of the compensation that will be made but also the events that will underlie when an NTC event will be called. This transparency will provide traders a means to react to any such market interventions.