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SEM Committee

Emer Gerrard

Simon O'Hare

Dear SEM Committee

The System Operator for Northern Ireland (SONI) welcomes the opportunity to respond to the Single Electricity Market Committee's (SEMC) consultation (Consultation Reference: SEM-23-024) on Compensation Arrangements for Net Transfer Capacity Reductions.

As Transmission System Operator for Northern Ireland, SONI plans, operates and co-ordinates the flow of electricity over the transmission system¹.

SONI TSO's position in this response represents our view of how the issues being consulted upon should most properly be addressed on a forward-looking basis only and nothing in this response should be taken as representing an indication or acceptance or otherwise of any rights and/or obligations of any market participants, interconnector owners or TSOs as they currently stand under the applicable regulatory and legal framework as at the date of this response.

SONI's response to the consultation is set out in the response below:

Question 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?

SONI TSO considers that the existing published regulatory framework for reduction in NTC compensation requires further updating. The Interim Cross Zonal Arrangements (ICZA), while sufficient and beneficial in terms of the initial establishment of SEM, clearly require further development in order to accurately capture the current existing capacity allocation process for SEM-GB interconnectors as well as to properly take account of applicable European law regarding capacity allocation. This further development was clearly contemplated within the express terms of the ICZA themselves as well as its accompanying cover letter published by the Regulatory Authorities.

¹ As per Condition 20(1) of [2022-11-18 SONI TSO Consolidated.pdf \(uregni.gov.uk\)](http://2022-11-18 SONI TSO Consolidated.pdf (uregni.gov.uk))

As noted in the consultation, the existing arrangements appear to address compensation with reference to the Forwards market that was in existence at the time of the launch of the new SEM rather than specifically with reference to the current interim arrangements where interconnector capacity is exclusively allocated in the Intraday markets. SONI considers it necessary that the ICZA is updated at least to accurately align with this existing capacity allocation mechanism.

SONI TSO undertakes a range of system security assessments on a daily basis to consider generation adequacy in Northern Ireland and in co-ordination with EirGrid TSO for the island. Any proposed regime that assumes that such actions generate an immediate compensation obligation against TSO's would appear to provide an unduly generous regime.

We note in particular that if SONI TSO is disincentivised to act in an expeditious manner to manage system security for the benefit of all users of the system (as it is required to do under its licence) due to a compensation obligation for NTC reductions, then there is a risk that this may generate a significant increase in Dispatch Balancing Costs (DBC) for energy consumers across the island and for Northern Ireland consumers in particular.

SONI TSO therefore considers the best regulation principles for NTC reduction is one in which the social welfare impact against consumers is minimised and TSO actions which reduce these social welfare impacts are constructively incorporated into the compensatory regime while of course respecting the applicable regulatory and legal frameworks. Such a process is critical as TSOs work to implement net zero policy targets while ensuring Security of Supply.

Creating onerous compensation obligations against SONI TSO has a wider damaging impact on Northern Ireland consumers. This arises due to the fact that interconnectors within SEM are dispatched based on their loss factor with interconnector assets with lower loss factors being dispatched first in the Ex-Ante market. As a consequence, and as noted in the SEMC paper, NTC Reductions to date are higher against the Moyle interconnector than against the EWIC interconnector. As a) both EirGrid TSO and SONI TSO actions and b) loss-based dispatch are implemented on an all-island basis, creating a larger compensation obligation against any one TSO in either jurisdiction appears unbalanced notwithstanding the higher congestion income that such dispatch principles when implemented will naturally generate for the relevant ICO.

SONI TSO therefore urges SEMC to consider that if dispatch of interconnectors and generation adequacy assessment within SEM continues on an all-island basis, then any compensatory obligation which arises (and which is in accordance with applicable EU law) should be distributed across both TSOs taking into account other factors such as revenue generation in both jurisdictions that will be similarly impacted by the existing loss-based dispatch.

SONI TSO notes that in the consultation paper the SEMC suggest that "*going forward, there may be a need to further optimise TSOs' obligations in terms of demonstrating or codifying need, reporting or transparency when they reduce NTC between GB and SEM*". SONI TSO considers that such a proposal is useful (and indeed would be within the contemplation of applicable EU law, including Commission Regulation (EU) 2017/1485) with "last resort" TSO actions completed to protect Security of Supply in advance of firmness deadlines excluded from compensation. SONI TSO considers that this is required to ensure that such actions undertaken under TSO licence are protected to reduce costs against NI consumers.

As above, SONI TSO considers that any future arrangements should immediately resolve ambiguity around intraday interconnector capacity allocation as a matter of priority.

Appropriate consultation on cross border hedging instruments if these materialise should be considered once the effective design of these instruments is known.

Question 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 SEM?

SONI TSO notes the range of terminology applied in this area both in EU and UK legislation and the difficulties associated with their transparent application across different market timeframes and under different scenarios. We recommend that clearly defined SEM specific legally defined terms should be published as part of the updated ICZA. Such terminology and associated compensation principles as above should acknowledge the role of TSO actions in reducing the social welfare cost impact of the energy transition to Net Zero and avoid any disproportionate allocation of these costs against NI consumers.

Question 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 noted in response to Question 2, SONI TSO considers that interconnector dispatch in SEM based on loss factors is an important additional factor for consideration by the SEMC. This is due to the fact that the use of loss factor for Ex-Ante dispatch creates both a disproportionate allocation of congestion income across both interconnectors and in this instance a higher compensation burden on Northern Ireland consumers (as the Moyle interconnector will be dispatched first in the market). Any proposed new ICZA rules needs to incorporate this factor into a consideration of how any material compensation arising should apply.

Yours sincerely

[sent by email and accordingly bears no signature]

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