



## **Single Electricity Market**

# **SMO Revenue and Tariffs: A Summary of Comments and Regulatory Authorities' Responses**

**31<sup>st</sup> August 2007**

**AIP/SEM/07/456**

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## EXECUTIVE SUMMARY

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A consultation paper on Single Market Operator (SMO) revenue and tariffs (AIP/SEM/246/07), published by the Regulatory Authorities on 11<sup>th</sup> June 2007, detailed and solicited comments on the Regulatory Authorities' proposals in relation to the form of SMO regulation<sup>1</sup>, the allowed revenue for the SMO, the cost of constraints, and all associated tariffs for the initial tariff period of the All-Island Single Electricity Market.

This response paper summarises and provides the Regulatory Authorities' responses to the comments that were received. It is intended to be read in conjunction with the associated Regulatory Authorities' decision paper on SMO revenue and tariffs (AIP/SEM/07/455), which is published in tandem with this paper and takes those comments into account.

In summary, comments were received in relation to the length of the initial tariff period, the form of regulation and performance indicators, the SMO allowed revenue, the imperfections charge, generator-under-test tariffs, and SMO charges and fees.

Comments that warrant a specific mention include those in relation to accession and participation fees as these resulted in a reduction in those fees. In addition, the Regulatory Authorities have provided further information in relation to SMO reporting requirements under the TSC, as this is relevant to a number of comments that were received.

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<sup>1</sup> The SMO is a contractual joint venture between EirGrid and SONI. It has been put in place to administer the All-Island Single Electricity Market which is due to commence operation on 1<sup>st</sup> November 2007.

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## **1. INTRODUCTION**

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### **1.1 FOREWORD**

This paper provides a summary of, and responses to, comments received from the public in relation to the Single Market Operator (SMO) revenue and tariffs consultation paper (AIP/SEM/246/07), which was published on 11<sup>th</sup> June 2007 by the Northern Ireland Authority for Utility Regulation and the Commission for Energy Regulation, together known as ‘the Regulatory Authorities’.

This paper should be read in conjunction with the associated Regulatory Authorities’ decision paper on SMO revenue and tariffs (AIP/SEM/07/455), which is published in tandem with this paper and takes comments received during the consultation process into account.

### **1.2 BACKGROUND**

The All-Island Single Electricity Market (SEM), due to commence operation on 1<sup>st</sup> November 2007, will be administered by the SMO, which was formed through a contractual joint venture between EirGrid and SONI, the transmission system operators in the Republic of Ireland and Northern Ireland respectively.

The SMO will need to recover from market participants its allowed operational costs, capital costs associated with the establishment of the SEM, constraint costs associated with the balancing of the transmission systems, and constraints costs associated with generator units which are being tested.

With a view to determining the allowed costs in the above areas, on 11<sup>th</sup> June 2007 the Regulatory Authorities published a consultation paper entitled ‘SMO revenue and tariffs’ (AIP/SEM/246/07).

The consultation paper outlined regulatory proposals on the form of SMO regulation, the allowed revenue for the SMO, the cost of constraints, and all associated tariffs. The paper solicited comments from members of the public, and these are now summarised in this paper along with responses from the Regulatory Authorities.

### **1.3 COMMENTS RECEIVED**

In total there were six respondents to the SMO revenue and tariffs consultation paper:

- Synergen,
- ESB Customer Supply (ESB CS),
- Airtricity,
- Viridian,
- ESB Independent Energy (ESB IE), and,
- The SMO

Section 2 summarises those comments and outlines the Regulatory Authorities’ responses. The comments have fed into the SMO revenue and tariffs decision paper (AIP/SEM/07/455), which has been published in conjunction with this response paper.

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## **2. SUMMARY OF COMMENTS AND RESPONSES**

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### **2.1 REGULATORY PRINCIPLES**

Only one respondent referred to the regulatory principles outlined in the consultation paper; it was felt that the principles are appropriate.

### **2.2 TARIFF PERIOD**

#### **2.2.1 Comments**

Five respondents (Synergen, Airtricity, ESB CS, ESB IE and the SMO) agreed with the proposed initial tariff period, that is, an 11 month control period from 1<sup>st</sup> November 2007 to 30<sup>th</sup> September 2008.

ESB CS highlighted their aversion to any adjustments to the tariff within the control period unless these adjustments were also aligned to within-tariff-period adjustments to end user tariffs. ESB IE also objected to the possibility of any intra-tariff-period adjustment. Confirmation was requested that no within-tariff-period adjustment will be allowed for the recovery of the imperfections charge.

The SMO requested that the Regulatory Authorities outline their views for the ongoing processes, particularly in relation to the length of subsequent tariff periods. The SMO also emphasised that any potential customer involved in the SONI divestment process would need firm commitments on future price controls to link with the proposed TSO five year<sup>2</sup> price control period commencing on 1 November 2007.

#### **2.2.2 Regulatory Authorities' Response**

The Regulatory Authorities acknowledge the respondents' satisfaction with the duration of the initial tariff period.

In relation to a within-tariff-period tariff adjustment (for the MO charges or the imperfections charge), the Regulatory Authorities are aware of the instability that such an adjustment would cause in the market and to suppliers in particular, and this is not considered desirable in the normal course of events. While the Regulatory Authorities cannot provide a cast-iron guarantee on this matter given the new nature of this market, the Regulatory Authorities have no reason to anticipate that a within-tariff-period adjustment will be required and will work to ensure that this is the case. One of the reasons for applying a relatively short timeframe for the initial SMO tariff period is to reduce any risk in this regard.

Regarding the length of the subsequent tariff period, the Regulatory Authorities have no firm view on this at present, though it is considered likely that its duration will be longer than the first tariff period. This will be considered further once the duration of the Northern Ireland TSO price control has been finalised.

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<sup>2</sup> The duration of the Northern Ireland TSO price control is currently under discussion between NIAUR and SONI and has not been finalised.

## **2.3 FORM OF REGULATION AND PERFORMANCE INDICATORS**

### **2.3.1 Overview**

On 11th June 2007, in addition to the SMO revenue and tariffs consultation paper (AIP/SEM/07/246) and the SMO revenue submission (AIP/SEM/07/247), a set of SMO performance metrics (AIP/SEM/07/248) were also published by the Regulatory Authorities.

These performance metrics were not intended to be used in relation to SMO financial incentives during the initial tariff period and were published for informative purposes.

Three respondents refer to these performance metrics; these and general comments on the form of regulation are detailed below. Individual responses are given to each comment.

### **2.3.2 Comments and responses**

#### **Comment**

Synergen felt that the performance metrics proposed by the SMO are insufficiently set out and do not contain readily measurable targets. Hence it was proposed by Synergen that the market participants' representatives and the SMO meet to commence the process of developing service level agreements and associated specific performance targets.

#### **Regulatory Authorities' Response**

The Regulatory Authorities will not use these performance objectives to provide financial incentives during the initial tariff period. Hence, while the use of these criteria will be given further consideration with respect to subsequent tariff periods, these criteria will not be further developed for use as financial incentives at this time.

However, given the above comments respondents may also be interested in providing input into a related consultation process. Under paragraph 2.144 of the Trading and Settlement Code (TSC) the SMO are required to produce and publish a report on a monthly basis. The Regulatory Authorities will carry out a consultation on the manner and extent of this reporting, and members of the public will be given the opportunity to comment. This may feed into performance incentives which will be considered for application in the next tariff period when more knowledge of the SMO's day-to-day operation is available.

The performance objectives published in conjunction with the SMO revenue and tariffs consultation paper (AIP/SEM/246/07) will also be reviewed by the Regulatory Authorities with respect to their suitability under the terms of the SMO licence (condition 10 for RoI and 16 for NI), which states:

'The licensee shall, in conjunction with the [licensee in the other jurisdiction], no later than SEM Go-Live, submit to the [relevant Regulatory Authority] for approval a report setting out the performance criteria against which the performance of the Single Electricity Market Trading and Settlement System may be measured'

However, these licence related objectives will not be subject to incentivisation during this initial tariff period.

**Comment**

Synergen also highlighted that points 11 and 12 of the performance metrics published in AIP/SEM/07/248 require the SMO to act outside its responsibilities as outlined in the TSC. It is stated that if the SMO considers that any additional activities are required as part of its support function within the TSC regime then the SMO should bring forward the relevant modification proposals to capture these requirements within the TSC.

**Regulatory Authorities' Response**

In principle, the Regulatory Authorities agree that activities funded through the SMO charges should not deviate from the support function outlined in the TSC. While these performance objectives will not be used to financially incentivise the SMO during the initial tariff period, Synergen's comments will be borne in mind when they are considered for use during subsequent tariff periods.

**Comment**

ESB CS sought clarity on how the performance of the SMO will be assessed.

**Regulatory Authorities' Response**

In relation to SMO costs, all costs incurred during the initial tariff period will be assessed *ex-post* by the Regulatory Authorities to ensure that the costs have been efficiently incurred. This assessment will feed into the SMO revenue consultation process for subsequent tariff periods, allowing the public an opportunity to comment on the *ex-post* assessment.

In addition, the SMO is required under the TSC to produce and publish monthly reports. While the content of these reports will be subject to a consultation process prior to being finalised, it is envisaged that they will cover the performance by the SMO of its rights, powers, functions and obligations under the TSC. This will aid in the assessment of its performance and will also assist in the implementation of suitable incentive schemes for subsequent tariff periods, if deemed appropriate.

In addition, the SMO licensees (EirGrid and SONI) are required, under the terms of their licences, to report annually to the respective Regulatory Authority on the performance of the Single Electricity Market Trading and Settlement System against performance criteria approved by the Regulatory Authorities. Further detail is provided above in response to the first query within this section.

**Comment**

Synergen states that the description of energy and capacity payments as cost-pass-through is incorrect and inconsistent with the TSC.

**Regulatory Authorities' Response**

It is acknowledged that all cash-flows, aside from SMO costs, are market-related and that the SMO administers these without being a principal, that is, a party to the transaction. Describing energy and capacity payments as 'cost-pass-through' was not meant to imply that the SMO is a principal, although such a description has no direct material impact. Rather it was meant to imply that the SMO is simply the administrative agent for these market-related costs over which it has no control. For clarity, and in order to ensure that the legal status of the SMO is clear, these references to 'cost-pass-through' refer to charges that are handled, or administered, by the SMO.

**Comment**

Both the SMO and Airtricity felt that the form of regulation was appropriate, with the SMO stating that they are in favour of developing an incentive programme for the next price control. ESB IE considered that metrics should be developed for this initial tariff period to form a base-line for future periods, and Viridian also stated that they would welcome the addition of a meaningful incentive scheme.

**Regulatory Authorities' Response**

The Regulatory Authorities agree that an appropriate incentive programme would be beneficial. However, given the start-up nature of this first period of SMO operation and the associated uncertainty, the RAs remain of the view that an *ex-post* assessment should apply to this first tariff period. An incentive programme will be considered for use during subsequent tariff periods, when there is more certainty regarding the SMO's operation.

It should also be noted that under the TSC and the MO licences, the SMO will be required to publish monthly reports and that these will assist in the setting of base-lines for incentive mechanisms that may be implemented during subsequent tariff periods (see Page 7).



## **2.4 ALLOWABLE REVENUE**

### **2.4.1 Overview**

This section outlines the comments received in relation to the *ex-post* review of all allowed SMO costs for the initial tariff period, financing costs associated with underpayments, SMO reporting requirements, currency costs, proposed new investments, Research and Development (R&D), operating costs, interest on working capital and Interest during Construction.

The SMO also stated that it believes the regulatory proposals on professional fees, facilities, IT & telecommunications, general & administrative, energy imbalances, other costs, Weighted Average Cost of Capital and the depreciation methodology used for the asset base are reasonable.

### **2.4.2 Comments and responses**

#### **Comment**

Airtricity indicated their agreement with the Regulatory Authorities proposal that the costs incurred during the initial tariff period be subject to an *ex-post* review.

The SMO requested that the timetable for the *ex-post* review be scheduled to allow for other resource constraints and also requested that the inflation methodology and capital expenditure be review *ex-post* to ensure appropriateness.

#### **Regulatory Authorities' Response**

The Regulatory Authorities will work with the SMO to ensure that a suitable timetable can be agreed for the *ex-post* review. All allowed costs related to the SMO, including the inflation methodology and capital expenditure, will be part of this review.

#### **Comment**

ESB CS commented that full automatic *ex-post* cost pass through of financing costs associated with underpayments to generators is not appropriate<sup>3</sup> and felt that market participants should not automatically finance the inefficiency of the SMO in relation to underpayments.

#### **Regulatory Authorities' Response**

The Regulators will be reviewing this cost *ex-post* to assess the validity and efficiency of these costs; they will not automatically be passed-through to market participants.

#### **Comment**

Airtricity proposed that a preliminary report on SMO revenue be made public (or at least market public) prior to the subsequent tariff period and that a full detailed report be made available at the end of the initial tariff period.

#### **Regulatory Authorities' Response**

During the initial tariff period a preliminary *ex-post* review will be carried out on all costs and this will feed into the allowed revenue for the subsequent tariff period. It is the Regulatory Authorities' intention that key information provided by the SMO on this issue will be published during the initial tariff period, in tandem with a consultation

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<sup>3</sup> This is detailed in Section 6.1.9 of the SMO revenue and tariffs consultation paper.

paper by the Regulatory Authorities relating to the allowed SMO revenues for the following tariff period. This will be followed by a decision paper on the matter.

Likewise it is the Regulatory Authorities intention that when the final *ex-post* analysis is carried out (this will be after the initial tariff period has ended when complete actual figures are available) the information provided by the SMO will also be published.

In addition, under the terms of the TSC, the SMO are required to produce and publish a monthly report as discussed in Section 2.3.2 of this paper. While the contents of these reports have not been finalised they are likely to contain information on SMO revenue.

#### **Comment**

ESB CS have stated that either the SMO or the Market Monitoring Unit should be tasked with monitoring constraint costs and providing regular reports and analysis. They feel that this should analyse actual costs versus budget and provide an analysis of the main generation receipts of constraint payments. This would provide transparency and provide a platform from which to launch a future incentive based scheme. While ESB CS recognises that incentives to reduce constraints are better placed on the TSO rather than the SMO, they request that the Regulatory Authorities signal their intentions to implement such a scheme in the near future.

#### **Regulatory Authority Response**

ESB CS comment in relation to the monitoring and reporting of constraint costs is noted. It is the Regulatory Authorities intention that these costs will be monitored under the SMO reporting requirements as per Section 2.144 of the TSC (Version 2.0). The contents of this report have yet to be finalised and will be subject to a public consultation process.

The longer-term objective of imposing an incentive based arrangement on the TSOs is outside the scope of this decision on SMO revenue and tariffs.

#### **Comment**

ESB CS stated that there will inevitably be a cost for currency fluctuations and request that these costs be identified and made transparent to the industry. Reference is also made to the fact that the TSC states that the SMO 'will endeavour to manage currency costs insofar as is practicable within the pool', and request greater clarity in this area.

#### **Regulatory Authorities' Response**

As above, it is envisaged that the SMO reporting requirements under the TSC will cover currency costs and that this will identify these costs in a transparent manner. These reports will be published by the SMO.

In relation to managing currency costs, as currency risk management is not a core skill of the SMO it would require specialist expertise that may not be cost effective. However, after market opening it would be sensible to re-examine the size and direction of currency flows and consider whether the requirements to 'manage currency costs insofar as is practical within the Pool' should include some form of currency hedging by the SMO for subsequent tariff periods

#### **Comment**

ESB CS queried how new investment will be considered within the tariff/price control and whether the SMO will provide a rate-case *ex-ante* for proposed major spends.

### **Regulatory Authorities' Response**

As referred to in the SMO's response to the Regulatory Authorities' consultation paper, once any future SEM related expenditure can be properly scoped, the SMO will then make a submission to the Regulatory Authorities in relation to that proposed expenditure. This submission will be assessed by the Regulatory Authorities.

In addition, under the terms of the SMO licence, the licensees must prepare and maintain a market system development plan for the development of the Single Electricity Market Trading and Settlement system over the following two years. The specific contents of this plan are currently being finalised. The year-one development plan is expected by 1<sup>st</sup> November 2007.

### **Comment**

The SMO stated that it finds the Regulatory Authorities' proposal in relation to R&D disappointing<sup>4</sup>, and highlights that this activity is not explicitly ruled out under any of the legislation, licences or the TSC.

A related comment, which is covered in Section 2.3.2 of this paper, highlights Synergen's concern that the SMO may act outside of its role as defined within the TSC, and states that if the SMO feel that additional activities are required then it should bring forward the relevant TSC modification proposals.

### **Regulatory Authorities' Response**

The Regulatory Authorities accept the SMO's assertion that a R&D activity is not explicitly ruled out by the relevant documentation. However, if it is not specifically required under the TSC, or is not required in order to allow the SMO to fulfil its obligations more efficiently, then market participants should not be required to fund the activity through the SMO tariffs.

### **Comment**

The SMO reiterated its belief that a small reduction in operating costs may reduce the SMO's ability to deliver its obligations and highlighted its disappointment at the reduced staff number proposed by the Regulatory Authorities. It also queried why their average proposed staff cost, based on currently allowed staff costs for EirGrid and SONI, was deemed unacceptable.

### **Regulatory Authorities' Response**

Both the Regulatory Authorities and the SMO acknowledge that it is particularly difficult at this stage to gauge authoritatively what level of resources will be required by an efficient SMO on an ongoing basis. In the absence of information which could allow a definitive assessment of whether the cost drivers behind each SMO function required the resourcing levels requested by the SMO, the Regulatory Authorities could not approve the full compliment of staff requested by the SMO. However, given the importance of the timely completion of this project the Regulatory Authorities proposed a reduced staff number which in conjunction with a contingency figure of €0.5m (to be reviewed ex-post), allows for a FTE compliment which is close to that sought by the SMO. This assumes that the average yearly staff cost is in line with that allowed by the Regulatory Authorities, rather than that proposed by the SMO.

In response to the SMO's second point, the currently allowed staff costs for EirGrid and SONI take into account the requirement for highly specialised staff to perform

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<sup>4</sup> The SMO had sought a provision of €0.3m for R&D. The Regulatory Authorities proposed that none of this provision be allowed as R&D is not a required function of the SMO.

power system operations and planning, a function that is not carried out by the SMO. Hence it is not appropriate to use the allowed staff costs for EirGrid and SONI as a basis for SMO staff costs.

Airtricity's comment that it believes the allowed SMO staff cost is in line with going market rates is also acknowledged.

**Comment**

The SMO has highlighted principles which they believe should apply in relation to the provision of interest on working capital. It requested that the interest provision related to under-recovery of revenue be determined using the Regulatory Authorities' assumed real cost of debt for the utility, as determined under the WACC. In relation to the repayment of over-recoveries, it was requested that an average 3 month Euribor rate adjusted for any differential between European HICP inflation and Irish HICP inflation be used for EirGrid's portion of the over-recovery.

**Regulatory Authorities' Response**

The methodology proposed for the provision of interest on working capital is consistent with the methodology used for the TSO functions that are carried out by EirGrid and SONI and there is no basis for using a different methodology for the working capital provided by the SMO. The methodology in relation to over-recovery is also in agreement with that which is put forward above in the SMO's response.

**Comment**

The SMO requested that an allowance for Interest During Construction (IDC) be included in the asset base. It is stated that in the normal course of events EirGrid and SONI would be allowed to recover their capital expenditure in the year in which it was incurred and as a result the issue of IDC would not arise. However, this is not the case with the SEM Programme, the cost of which has been borne by EirGrid and SONI since 2005. This has resulted in EirGrid and SONI adopting the principle that applying IDC to actual spend is both appropriate and reasonable. EirGrid and SONI further believe that IDC has two components, the opportunity cost of the finance used but not recovered, and its time value.

**Regulatory Authorities' Response**

Following a review of the SMO's request the Regulatory Authorities have included an allowance for IDC in the SMO asset base. The details of the review, the request that was submitted by the SMO and the allowance made by the Regulatory Authorities are covered in the SMO revenue and tariffs decision paper.

## **2.5 IMPERFECTIONS CHARGE**

### **2.5.1 Comments**

Viridian expressed surprise at the magnitude of the SMO charges and the imperfections charge, and suggested that there should be a related reduction in system related charges. It was also suggested that an explanation by the Regulatory Authorities to customers would allay any perceptions that this is a new charge.

Viridian further highlighted that there could be public sensitivity to a common All-Island imperfections charge, if there was a perception that the underlying costs arise predominantly in one jurisdiction.

ESB IE also expressed support for the proposal that constraint payments should not be withheld from Generators<sup>5</sup>, as this would create market instability.

### **2.5.2 Regulatory Authorities' Response**

The costs to be recovered through the SMO charges have been detailed and explained in the SMO Revenue and Tariffs consultation paper, Section 6, and the Regulatory Authorities are working with the respective TSOs to ensure that allowed revenue for functions which have transferred from the TSOs to the SMO are not also recovered through EirGrid's/SONI's Use of System charges in the new market.

For example, EirGrid's allowed payroll cost for the period from 1<sup>st</sup> November 2007 may be adjusted downwards due to the transfer of certain functions to the SMO and the EirGrid Use of System charges may be adjusted accordingly from 1<sup>st</sup> November<sup>6</sup>.

The same is also true for costs associated with the imperfections charge. However, in some cases the imperfections charge merely replaces cash-flows within the current market that are associated with constraint payments, rather than a distinct element of Use of System charges.

It should also be noted that when comparing individual cost elements of the SEM to those of current market arrangements it is important to view all costs within the context of the overall benefits provided by the SEM, including the competition, security of supply and efficiency benefits gained from the combination of two smaller markets into a single All-Island arrangement.

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<sup>5</sup> In their revenue submission the SMO proposed that in some instances, where exceptional level of constraints arose, the payments of constraints would be withheld pending an investigation into the validity of these levels of payments. However, this is not facilitated under the TSC.

<sup>6</sup> This will be subject to consultation prior to being finalised.

## **2.6 GENERATOR-UNDER-TEST TARIFFS**

### **2.6.1 Comments**

Two comments were received in relation to generator-under-test tariffs. Airtricity signalled their agreement with the proposed option, a MWh charge that is banded by capacity. Synergen suggested a simple MWh charge on the basis of simplicity as they state there is no evidence that this is not cost reflective.

Synergen also requested that the modelling be published as part of the next phase of consultation.

### **2.6.2 Regulatory Authorities' Response**

Airtricity's agreement with the proposed option is noted. In relation to Synergen's comment, the System Operators have stated that a banded tariff is more cost reflective since generator-under-test tariffs reflect the increased costs incurred as a result of altering the TSOs' operating policy to manage a unit under test, and while small/medium sized units under test might not alter the normal reserve requirement larger units would. Therefore, as per the option proposed in the consultation paper, the Regulatory Authorities have decided to implement a €/MWh charge that is banded by capacity for the initial tariff period.

The basis behind the calculation of these tariffs is detailed in the accompanying SMO revenue and tariffs decision paper (AIP/SEM/07/455).

## **2.7 SMO CHARGES AND FEES**

### **2.7.1 Overview**

A number of comments have been made in relation to:

- fixed and variable SMO charges, and,
- participation and accession fees.

These are outlined in Sections 2.7.1.1 and 2.7.1.2 respectively.

#### **2.7.1.1 SMO charges: Comments and Regulatory Responses**

##### **Comment**

A number of comments were received in relation to the allocation of costs between the fixed and variable charges.

Airtricity welcomed the Regulatory Authorities' proposal that the majority of all costs be recovered through the variable charge. The SMO also stated that it accepts the approach to tariffs proposed by the Regulatory Authorities<sup>7</sup>.

However, another respondent, Synergen, stated that no data analysis or economic rationale has been presented to support the allocation for fixed charges and propose that the fixed charges be set to zero. They state that the low fixed charge proposed by the Regulatory Authorities will result in administrative costs that outweigh the benefits of charging. Their proposal would address this and also remove any risk premium incurred by generators to convert the fixed amount into a €/MWh figure.

Viridian also suggested that fixed charges to suppliers be set to zero, as the application of such charges could reduce incentives for customers to lower their energy consumption.

A fourth respondent, ESB CS, stated that the allocation of 95% of costs to the variable charge is not equitable for suppliers and that fixed charges should recover fixed costs with variable charges recovering operational costs. They also query how a significant portion of the costs are classified as variable.

##### **Regulatory Authorities' Response**

To provide clarification, it should be noted that the approach proposed in the consultation paper does not classify costs as variable; it instead allocates costs to be recovered through the €/MWh or variable charge.

As reflected by the above comments a number of approaches could be taken when allocating SMO costs to be recovered through fixed or variable charges. Most respondents either accepted the methodology proposed by the Regulatory Authorities in the consultation paper, or accepted the principle that the majority (or all) of the costs would be recovered through the €/MWh variable charge.

One respondent highlighted another option whereby all capital costs would be recovered through the fixed charges. The Regulatory Authorities presume that this option is based on the assumption that all other costs are MWh driven, whilst capital costs (or the depreciation related to capital costs) are assumed to be a function of

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<sup>7</sup> A minor revision is proposed in relation to participation fees as outlined in Section 2.7.1.2.

system size, itself driven by the number of generator and supplier Units that the market must cater for. While these assumptions in themselves could be subject to debate, one main counter-argument is that since the market as a whole benefits on a per MWh basis from these SMO costs being incurred (due to the improved commercial environment for the purchase and sale of electricity), this benefit should be reflected in the €/MWh variable charge, rather than the fixed charge.

Two respondents stated that the fixed charges should be set to zero, with one stating that the administrative costs would outweigh the benefits of a small fixed charge. With respect to this comment, the Regulatory Authorities expect that if it is practical and more efficient to amalgamate the invoicing of fixed SMO and other charges, then the SMO will do so. The second respondent stated that the application of a fixed charge would reduce the incentives on consumers to reduce their energy consumption. However, the potential impact of this is reduced by the relatively small scale of the fixed charge.

#### **Comment**

Airtricity stated that while they welcome the proposed allocation of costs between the fixed and variable charges they disagree with the basis for the fixed MO charges to generators. The Regulatory Authorities proposed that the fixed charge to generators would vary according to the installed capacity of generator Units, but Airtricity feel that this is not an equitable treatment of generators given the benefit that different generators receive from the SEM. They proposed that a factor related to the historical average load factors of the different generator types be used to calculate fixed MO charges as they state this would be more reflective of the different revenue streams received by generators. The basis for the proposal is published separately within Airtricity's response to the consultation paper.

#### **Regulatory Authorities' Response**

The approach proposed by the Regulatory Authorities for the fixed MO charge to generators reflects differences in the revenue streams of generators with different installed capacities. Airtricity's proposal would go one step further by allowing for fixed charges to vary based on differences in the capacity payments received by the different generator types with similar installed capacity.

Airtricity's proposal assumes that the revenue streams of generators with the same installed capacity will only vary according to the differences in capacity payments received (with a thermal unit receiving capacity payments for its total installed capacity and a wind generator receiving capacity payments for its actual output). However, energy payments will also vary depending on whether a generator is base-load, mid-merit and peak. Accordingly, if the fixed MO charge to generators was varied to allow for the differences in capacity payments received, then it should also be varied to allow for differences in energy payments received. This would not be practical and therefore the Regulatory Authorities' have not changed the approach based on Airtricity's comment.

#### **Comment**

The Regulatory Authorities proposed that the fixed charge to generators would vary according to the installed capacity of generator Units. Airtricity requested that clarification be provided as to how installed capacity would be treated for special Units such as an interconnector Unit.

#### **Regulatory Authorities' Response**

In relation to interconnector units, the TSC, Version 2.0, Section 7.20 states:



*Until the date that is 12 months after the Market Start Date, the following paragraph shall be inserted after paragraph 6.143:*

*'6.143A The Fixed Market Operator Charge shall not apply to Interconnector Units or to Interconnector Error Units or to Interconnector Residual Capacity Units.'*

For demand side Units, the fixed market operator fee will be set to zero.

### **2.7.1.2 Accession & Participation: Comments and Regulatory responses**

#### **Comment**

Airtricity highlighted their uncertainty regarding how participant training costs are being recovered and requested clarification that there is no double accounting of participant training costs.

#### **Regulatory Authorities' Response**

The Regulatory Authorities and the SMO are working together to ensure that there is no double accounting for all costs. In relation to the costs associated with participant training prior to SEM Go-Live, a decision paper published by the Regulatory Authorities entitled: 'Decision on the treatment of accession and participation fees during the pre Go-Live period' (AIP/SEM/312/07) should address the respondent's specific concerns in relation to participant training costs. That paper states that accession and participation fees will not be charged in relation to parties and Units that were registered for market trial.

#### **Comment**

Airtricity believe that the Full Time Equivalent (FTEs), including legal resources, required to carry out the specific steps within the accession and participation processes have been overstated. They also feel that the FTE charge out rate used to calculate the fees are not reflective of going market rates. Airtricity provided an amended breakdown of the time requirements for the accomplishment of these processes, and used a revised FTE charge out rate, based on the Regulatory Authorities' proposed allowed payroll costs, to calculate accession and participation fees which they feel are more cost reflective.

The SMO has also proposed a revision to the participation fee. In light of recent developments to related agreed procedures and business processes, and a more complete understanding of the workload required to complete the registration process, the SMO proposed reducing the participation fee to €7,000 (for suppliers and generators). This is based on 14 FTE days and a call out rate of €500 per day.

Both proposals are detailed in the respective comment papers, which are published in conjunction with this response paper.

#### **Regulatory Authorities' Response**

The Regulatory Authorities welcome the reduced participation fees proposed by the SMO which reflect the change of scope for the registration service.

The Regulatory Authorities have noted Airtricity's comments on the accession and participation fees. Airtricity felt that the cost of a FTE used by the SMO to calculate the fees (€500 per day) was not reflective of going market rates, and proposed a fee based on a FTE cost of €362 per day. This is in agreement with the staff cost of €80,000 per staff member per annum proposed by the Regulatory Authorities. However, the figure of €362 (and the corresponding annual staff cost of €80,000) only takes salary costs, pension costs, *et cetera* into account and does not allow for

other costs, such as facility costs which are related to the staff member. Therefore the Regulatory Authorities have continued to use the daily FTE cost of €500 proposed by the SMO.

Airticity also highlighted uncertainty regarding the time requirements needed by the SMO to fulfil the accession and registration processes. To allow for Airticity's comment, the Regulatory Authorities have decided to implement reduced accession and participation fees as detailed in the SMO revenue and tariffs decision paper.

It should also be noted that these fees are one-off (per party for accession and per unit for participation) and, as noted by the SMO, the Regulatory Authorities have recently decided that there will be no charge to parties or Units that participate in market trials<sup>8</sup>. For subsequent tariff periods the scale of these fees will be revisited.

## **2.8 OTHER COMMENTS**

### **Comment**

Viridian stated that they would like further debate on to the identity of the party that delivers certain market function such as market modelling and market monitoring.

### **Regulatory Authorities' Response**

Viridian's comment is acknowledged but these topics are outside of the scope of this SMO revenue and tariffs consultation process.

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<sup>8</sup> Decision on the Treatment of Accession & Participation Fees during the pre Go-Live period (AIP/SEM/312/07)

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## 5. SUMMARY

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Six sets of comments were received in relation to the SMO revenue and tariffs consultation paper. These are summarised in this paper and have also been published in full in conjunction with this response paper<sup>9</sup>.

In addition to providing Regulatory responses in this paper, the comments that were received have also fed into the Regulatory Authorities' SMO revenue and tariffs decision paper (AIP/SEM/07/455). This document has also been published in conjunction with the response paper.

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<sup>9</sup> [www.allislandproject.org](http://www.allislandproject.org)