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RE: EAI response to SEMC consultation on Financial Transmission Rights (SEM 15061)

Dear James/Joe,

EAI members welcome the opportunity to engage in this I-SEM workstream concerning the allocation of interconnector capacity between ISEM and its connected markets via Financial Transmission Rights (FTRS) from ISEM go-live in April 2017. A number of the questions raised in this consultation are the subject of ongoing determination at a regional/European level. The recently established Joint Allocation Office (JAO) is intended to represent the enduring European solution for a single allocation platform underpinned by the Forward Capacity Allocation Code (FCA) and Harmonised Allocation Rules (HAR). It is our understanding that JAO will be in a position to facilitate FTR options in April 2017 but the availability of FTR obligations on JAO will be delayed beyond I-SEM go-live pending finalisation of the FCA and HAR. Whilst EAI supports progress towards the enduring solution we seek clarification on whether this limitation rules out obligations if the JAO is used for the first FTR auction in April 2017 and therefore whether a regional/local solution is required to retain scope for options and obligations at ISEM go-live.

In light of the uncertainty outlined above, we would caution that optionality and flexibility be retained in the ISEM design to allow for the ongoing evolution of the EU rules. We would also advocate an ISEM solution that is not overly complex, clearly understood by domestic/regional stakeholders and not subject to onerous collateral requirements. We seek an holistic approach across all ISEM workstreams to ensure that collateral requirements are understood and minimised for participants. EAI is working with Eurelectric to ensure that FTRs are classified as physical products and therefore not subject to regulation relevant to financial derivative products.

In relation to the questions posed in this consultation, EAI does not support discounts on FTR payouts for losses, ramping and curtailment and supports a single FTR at the ISEM trading boundary.

1 Options v Obligations;

- EAI does not have a strong preference for one over the other and we recognise the pros and cons of both.
- Clarification sought on interaction between this decision and auction platform

2 A single FTR at border vs separate for EWIC and Moyle;

EAI has a preference for a single FTR to apply at the I-SEM trading boundary. A single FTR, subject to the position outlined in 3 below, would be less complex/costly for participants and would concentrate liquidity.

We seek further evidence to justify the SEMC 'minded to' position for separate FTRs, specifically the contention that the collaboration costs incurred by the interconnector owners (ICOs) would outweigh the benefits that might accrue from a single FTR.

We also note that The Agency for the Cooperation of Energy Regulators' (ACER) 2014 market monitoring report observes that multi-market transmission products could benefit smaller bidding zones (providing access to more liquid trading 'hubs'). If this is a desirable outcome of the IEM, development of such products (even if they developed on a step wise basis) would occur more readily where single products are available at borders.

3 Discounts

EAI does not support discounts on FTR payouts for losses, ramping and curtailment.

As a financial product, FTRs act as a risk management tool for market participants, seeking to hedge the differential between two prices. Discounting for losses will increase complexity, reduce the effectiveness of cross border hedging strategies and therefore negatively impact forward liquidity for I-SEM. Should the SEMC proceed with its minded to position of including a discount for losses, those losses should be fixed and notified to participants in advance so bids can be adjusted accordingly.

The inclusion of ramping and/or curtailment in FTR products would further increase the unmanageable risks imposed on participants (because they cannot be accurately forecast at time of capacity procurement). We await further detail on curtailment in the EU Guidelines but note the importance of an appropriate definition of curtailment to ensure it is not extended to include things incurred through normal business operation of ICs, like testing or obligations imposed through delivery of system services (e.g. black start capability)

Finally, EAI is very concerned about the current drafting of Annex 12 in the voluntary HAR document. Specifically, we do not agree with the attempt by the SEM ICOS to maximise the number of situations in which they can declare a curtailment event and consequently widen the situations for which they can cap curtailment compensation for FTR holders. Such an approach significantly undermines the value market participants could place on FTRs as hedging instruments and undermines the usefulness of cross border trading as a risk mitigation tool for congestion and pricing risks. EAI requests significantly more consultation on this issue before the situations in which curtailment compensation caps can apply are finalised pursuant to the Forwards Capacity Allocation guideline and the related Harmonised Allocation Rules (HAR).

EAI members would welcome the opportunity to discuss this consultation response in further detail.

Yours sincerely,
Stephen Douglas
Senior Advisor
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