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RE: SEM-20-044 System Services Future Arrangements Scoping Paper (the “Paper”)

2nd October 2020

Dear Dylan and Bronagh,

Bord Gáis Energy (**BGE**) welcomes the opportunity to respond to the SEM Committee’s (SEMC’s) scoping paper on the System Services Future Arrangements to apply from 1 May 2023. This cover letter outlines our key points and the appendix to this letter goes into additional details on certain matters in line with the questions raised in the Paper.

1. A decision on a robust, timely framework

In the context of the 70% renewables in electricity and decarbonisation targets for 2030, it is **critical that a tested enduring framework for procuring system services for application once the current regulated arrangements end, is designed and introduced as early as possible**. System services are a necessary complement to the roll-out of renewables. Low-carbon existing and developing technologies including CCGTs, demand-side-response and batteries for example, are and will play a key role in the provision of system services. The chosen framework should facilitate investor certainty which calls for early notice of a confirmed date for a change in arrangements, early decision of the extent of the change and clarity on governance. The current regulated arrangements under which the majority of system services providers are operating have provided a stable basis for revenue predictability, but the EU policy and regulatory landscape is changing, and the expediency and reactivity of system service providers needs to adapt accordingly. Ultimately, we believe that the RAs should seek to align with the EU legislative requirements¹ as quickly as possible and that consideration of a move to daily auctions from 1 May 2023 pre-ceded by appropriate trials merits consideration.² BGE is in favour of competitive auctions that deliver the most cost-effective efficient outcomes for consumers. A balance needs to be struck between a) consumer value, b) maintaining security of supply, and c) avoiding inefficient exit of units necessary for decarbonisation aims. We believe that moving to daily auctions has the potential to achieve this balance.

We discuss in more detail in our answer to question 3 the objective and assessment criteria proposed by the RAs to apply to this project. Security of supply (under “system need”) goes to the crux of the purpose of system services. The prospect of a move to daily auctions and one-day contracts from our current regulated arrangements is a change but not an insurmountable one. These auctions are already in operation with great success in mainland Europe. We support the move to such daily auctions and believe that the current regulated tariffs could act as a fallback pricing solution should there be any barriers or issues during the initial stages in the auction roll-out. The “Alignment” assessment criterion³ alludes to taking a holistic view of the three main revenue streams – energy, capacity and system services – when determining the enduring system services framework. We believe that the Alignment criterion is key to ensuring that efficient exit signals are retained across the markets while ensuring that inefficient exit is avoided. Simultaneously **the Alignment criterion will put pressure on service providers to adapt to ensure their efficiencies and capabilities of providing system services are in line with the EU vision of short-term markets and competitive costs for services** which costs are as low as possible for consumers.

¹ As outlined in the Paper

² Post-implementation ongoing review should occur, and scope should be retained to make appropriate adjustments to ensure auctions are functioning as intended and expected

³ “The SEM Committee will seek to ensure appropriate alignment between the markets in energy, capacity and System Services, along with all other relevant revenue streams, to ensure an efficient overall outcome for consumers”

The Regulatory Authorities (**RAs**) would be better placed to make an informed decision on the timing of a change from the current regulated arrangements and on the appropriate format of the procurement approach for each of the 14 system service (and future) products if **the TSOs and DSOs, with the support of the MMU, provided an estimate on the volumes needed for the existing 14 defined system services**. The volumes needed would ideally be depicted on an annual basis from 2023-2030. The product volumes' estimate should also include a view on the shortage of products and locations of shortages. BGE recognises that the need for some of these services could fall away or new system service needs could arise, but the starting point must be the system services we know that we currently require and will require at least in the short to medium term. Similar analysis to that included in the 2014 System Services Decision Paper, whereby the required increase in installed capability to achieve SNSP of 75% is depicted, would meet this ask and such a report would align well with one of the RAs' proposed assessment criterion, "Accuracy: The volume of services procured should match the requirements of the system as accurately as possible".⁴ **BGE believes that an early decision on the timeline for any change to the current regulated arrangements is required by Q1 2021 to assist investment decisions**. Ideally a clear implementation plan with milestone dates would be issued in parallel with a decision on the timeline for implementing auctions, but a decision on the latter is more pressing.

2. Regulatory intervention

Related to the above points on the determination of product volumes asap by the TSO and investor certainty is the extent of the need for regulatory intervention to ensure consumer value. While on the face of it some system service products may have an obvious market power issue, **we believe that the default starting design position should be that no price caps or bidding rules are necessary for products/ product bundles until the potential for market power abuse to the detriment of competition and the consumer is robustly evidenced**. This evidence of potential to exercise market power abuse can be informed by the TSO/ DSO analysis we request in point 1 above. The evidence used to inform the extent of any regulatory intervention could for example include determination of (a) the volumes of the 14 products required at certain points in time, (b) the locations in which these products are required, (c) the number of market participants in a position to offer these products in these locations, (d) whether the products are for the transmission and/ or distribution system. BGE supports regulatory intervention where the need for such is robustly evidenced and with the above suggested list of information, we believe the RAs can make informed decisions that ensure competition puts pressure on prices for the benefit of consumers. Where there is a strong risk that competitive pressures will not exist then appropriate, targeted (and of limited duration) intervention could apply. Any regulatory intervening measures that are ultimately determined as necessary for consumer protection should also be designed with a view to protecting against inefficient exit of units as well as facilitating investment decisions for units required to support long-term decarbonisation.

3. Contract durations and avoiding a two-tier system services market

BGE is in favour of auction-based procurement as competitive auctions should deliver best value for the consumer. An immediate change from regulated arrangements to daily auctions with one-day contracts could be feasible if sufficient notice of the change in date to auction procurement and the design and format of those auctions is forthcoming. Our understanding of the EU legislation under scrutiny in the Paper is that frequency-based and reserve products such as POR, SOR, TOR1, TOR2, RRS, RRD fall under the EU definition of "balancing capacity" products. As such, these six system services must be considered for daily auctions with contracts of one-day duration. We have a concern that if a derogation from the daily auction/ one-day contract requirement is obtained by the RAs, the derogation can only apply to 60% of volumes thus 60% of the volumes procured may be under one set of procurement arrangements while the remaining 40% would be under the daily auction/ one-day contract procurement requirement. It is unclear how these volumes would be distinguished and what possible market distortions might arise but we request the RAs' views in the next detailed consultation on the delineation of how volumes that could be subject to any derogation from the EU provisions could be distinguished and how the risk of insufficient system services being procured under auction arrangements (>40% of volumes) versus under the alternative / derogation arrangements (60% of volumes), could be mitigated. **BGE believes there is considerable merit in adopting auctions in May 2023 with a preceding trial period without seeking any derogation for balancing capacity products and this would avoid the risk of the two-tier system services market, at least in the balancing capacity products noted above, potentially arising**.

⁴<https://www.semcommittee.com/sites/semcommittee.com/files/media-files/SEM-14-108%20DS3%20System%20Services%20Decision%20Paper.pdf> p.20 Figure 4. Figure 5 of the same paper outlines an assumption of the various technologies that can offer a portion of the respective products which is also insightful

Based on our understanding of the operation of the auctions, if an auction results in a commitment of a duration longer than one day we believe that the design process for system services must **consider risk mitigation e.g. secondary system services trading options**, when service provision is committed but the unit needs to trade the obligation out due to a forced outage for example.

In general, a technology neutral framework is the preferred approach in any solution. In light of decarbonisation targets however we believe that, again based on evidence from the TSOs/DSOs of volumes of products required by particular dates and the existence of service providers to provide such products **consideration of longer-term contracts for certain developing technology types may be merited. It is necessary however that strict criteria apply** in that these long-term contracts are allocated only to new technologies that prove that their main focus is grid support services and that they are reliant on system services revenue for a specified high percentage of overall revenues. **BGE is not however in favour of offering long term contracts due to a lack of sufficient competition in an area** – scarcity scalars currently exist to cater for this in the Dublin area – long term contracts would lock consumers into paying for higher priced system services on a long term basis stifling the potential growth of competition in the system service(s).

4. Auctions - which products and a single design

Auction-based procurement on a system wide basis should be possible for both frequency-based and non-frequency-based system services. It is not straight-forward or appropriate to simply decide that for example non-frequency services such as voltage and inertia are not suitable for system-wide auctions. Inertia for example is a system wide issue and could be procured in system wide auctions. We understand however that there are certain inertia related bilateral contracts that are not yet considered capable of system-wide procurement and we request that where steps can be taken to broaden the pool of potential system service providers of a particular product, they are notified to the RAs and to the market as soon as possible.

Where system wide auctions put securing the required volumes of a system service(s) at risk whereby either security of supply or efficient cost-effective procurement is undermined, this must be robustly evidenced by the TSO/ DSO in line with our request for insights on volumes needed for 2023-2030 under point 1 above. Voltage needs in some areas may be one example of localised procurement requirements. **BGE is not in favour of bilateral contracts for any system service primarily as they counter the consumer value criterion and greatly undermine competition.** Where the TSO can evidence the extent of a local system service problem and any limits on competition that could undermine outcomes that deliver value for the consumer, alternative solutions should be considered in parallel to considering alternative competitive procurement of system services. Taking the Greater Dublin area for example, our understanding from the Locational Scarcity Scalars papers⁵ is that the Dublin constraints issue (which limits the breadth of market participants that can contribute to alleviating Dublin's voltage issues) will be resolved by 2027. In the meantime, grid solutions such as the installation of static devices can help the issue together with the planned reinforcements for Dublin to alleviate constraints. Considering the already localised nature of the locational scarcity scalars (benefiting Dublin only units), **BGE is not in favour of additional system service-related payments (beyond the existing locational scalars) benefitting only units that are based in Dublin. Any solution adopted under the future arrangements to ensure security of supply in Dublin at least cost for the consumer, should a) first consider how market participants both inside and outside Dublin can competitively contribute to the solution; and b) be designed in a manner that does not negatively commercially impact units based outside Dublin (which impact is a real probability due to the payment basis of the current locational scarcity scalar for 4 of the 6 system services).**

In terms of the use of auctions as a procurement approach for all system services, we recognise the difficulties in implementing a fully market-based approach due to an insufficient level of competition. Again, an informed decision on the appropriate procurement approach across all system services would be best enabled by a detailed view from the TSOs/ DSOs on the volumes of the current 14 system services required over 2023-2030. In general, however, when there are **products for which an auction approach is determined as suitable, then the same auction format should apply across all of these products**, i.e. one auction design such as a demand curve which sets a clearing price relative to volumes on the system, should apply no matter what the product is. Constraints should not influence the clearing price – a single clearing price per product/ bundle should apply. We believe that this principle of the same auction format design and operation applying to all products, can apply regardless of whether some products are “bundled” (e.g. reserves products) for auctions or not. A uniform auction format would best achieve the “simplicity” criterion⁶ proposed for this process.

⁵ E.g. <http://www.eirgridgroup.com/site-files/library/EirGrid/DS3-System-Services-Locational-Scalars.pdf> p.5

⁶ “framework should be sufficiently simple and transparent to be readily understood and accessible to all stakeholders”

5. System services – product bundling

When it comes to determining the suitability or not of bundling products together, BGE believes that there is scope to bundle reserve products together at least, considering the technical nature of the provision of primary operating reserve (POR) for example is linked to the incidental provision of other reserve products which provide valuable service to the TSO/ DSO and consumers. Compatibility of products and bidding rules where applicable is necessary before bundling. **We believe however that caution should be exercised around the appropriate choice of which products to bundle or not - the optimisation function that will apply in the finally chosen procurement method must be transparent, predictable and allow market participants to replicate and validate outcomes** with a view to informing existing, amended and new business cases. Such validation could for example be undermined where products are bundled with other products to which different market power controls may apply. BGE is not in favour of solutions that will render pricing and commitment outcomes unverifiable or unpredictable.

6. Capacity to provide system services should be informed by energy market outcomes - timing

The procurement of system services should remain separate to the ex-ante and balancing energy markets. Provision of System Services should not determine how a market participant should operate in the energy market; **a market participant should reflect its capability to provide System Services based on how they intend to run in the Energy market.** In this context therefore, BGE favours a solution that sees market-based procurement of system services occurring after day-ahead market results are known. Procuring system services in this manner for example would allow an informed view of reserve requirements given that the largest single infeed, known on DAM results, informs reserve levels. This in turn would help ensure the appropriate level of reserves is procured to deliver value for consumers. If daily auctions with one-day contracts were adopted a potential increase in intraday market liquidity may also be seen whereby market participants buy and sell more volumes in a bid to account for their system service commitments. Procuring system services where market participants have energy market results is also closest to what we have today which could be conducive to a smooth transition to auction-based arrangements. Furthermore, given the current SEM pricing and settlement issues we are experiencing we do not believe there is any merit in considering co-optimisation of system services with the balancing market.

7. General

Our understanding is that the future system services auctions would be administered by the TSOs. BGE believes that the TSOs should be adequately resourced to deliver a move to auction procurement of system services within the Electricity Price Review 5 period of 2021-2025. Please see our response to the CRU's PR5 consultation which closed in mid-September – **appropriate groundwork to achieve 2030 aims must be made by the TSO before 2025 but the costs must be evidenced and justified and notified annually** when any change in over/ under spend occurs.

BGE suggests that a **short consultation on the appropriate terms of reference for this system services project would be beneficial.** Our initial views are that the terms of reference should at a minimum require: sufficient and robust consultation with industry with consultation durations of 4-6 weeks depending on the subject matter; that a holistic view of the need to maintain security of supply together with achieving decarbonisation aims in a manner that mitigates inefficient exit while allowing investment decisions to be taken with a view to protecting the consumer and delivering value, is applied; a rules liaison group with the Q&A approach that was adopted for the I-SEM project be established; that independent certification of any auction algorithms and accuracy of outcomes including settlement and pricing is obtained before go-live; and that transparency and predictability of outcomes such that outcomes and prices can be replicated and validated will be ensured with a view to smoothing the transition for investors from the current regulated arrangements to an auctions-based approach while maintaining value for the consumer.

We commend the RAs' organisation of the two webinars that occurred during this Paper and noted that the TSOs plan to issue their view on how the system services arrangements could operate in early October. **We request that the RAs and TSOs publish the TSOs' view as early as possible** such that industry has early sight of proposals and can share views perhaps via a webinar before the RAs issue their next consultation on future system services arrangements in Q1 2021.

The above suggestions and comments reflect our main concerns and thoughts on how this system services workstream and the design of the arrangements should progress with a view to achieving daily auctions for May 2023. Our answers to the questions raised in the Paper are outlined in the Appendix immediately below and build

on the above commentary. I hope you find this response helpful and BGE looks forward to engaging with the RAs over the coming months to determine a solution that achieves the appropriate balance between consumer value and protection and certainty for investors that are necessary to achieve decarbonisation in the short-long term.

Yours sincerely,

Julie-Anne Hannon
Regulatory Affairs – Commercial
Bord Gáis Energy

{By email}

Appendix – Answers to Questions in the Scoping Paper

1) Are there additional requirements in EU legislation or national policy that should be considered as key guidance for the project?

BGE believes that the Paper has made adequate references to various targets and ambitions in the Irish and EU policy and regulatory landscapes that capture the extent of the change required to system service procurement approaches and the rationale for these changes.

EU policy and regulatory requirements are changing, and system service providers in Ireland need to adapt.

We have outlined in our cover letter above our concerns on the creation of a two-tier system services market if a portion of reserves products are granted a derogation. Due to this potential derogation only applying to a maximum of 60% this means that at least 40% of relevant balancing capacity products must comply with the daily auctions with one-day-contract requirement. In order to mitigate against the risk of a two-tier procurement approach, we believe that daily auctions from 1 May 2023 should be pursued with the current regulated tariffs providing a fallback pricing solution should there be any barriers or issues with the initial auction roll-out. The auctions should be preceded by a trial and following implementation should be continuously reviewed to ensure their operation is in line with the design.

2) What should the role of DSOs be in development of the new arrangements?

BGE believes that strong TSO/ DSO collaboration will necessarily be required to deliver the system services needed to ensure the decarbonisation objectives for 2030 are achieved. Network development will certainly be complemented with distribution level system services. The DSO should be heavily involved in the high-level design and subsequent detailed design phases such that local system service solutions e.g. around congestion, are integrated with TSO solutions at least cost to the consumer. Where products are common to the TSO and DSO consideration could be given to a common bid list allocated to either transmission or distribution system services – the clearing algorithm could ensure a sufficient amount of service is allocated for both systems – a simultaneous market clearing should ensure the lowest procurement cost of the system service. Enhancements in TSO/ DSO communications systems will also likely be required to ensure that both system operators have up to real time information on services provision on both systems.

3) Should any further assessment criteria be included in this workstream?

Yes. Consumer protection in terms of ensuring continued value for consumers in system services provision is important. A move to auctions will facilitate achievement of the consumer criterion. A holistic view on the three main revenues streams⁷ together with other applicable sources of revenue is required to protect against inefficient exit of units but it should also be borne in mind that moving to daily auctions will put pressure on system service providers to adapt and become a more active provider of system services. The need to facilitate investment decisions for newer technologies should also be borne in mind. System services providers becoming more active in system services provision is in line with renewables and decarbonisation aims as well as being in line with the Clean Energy Package's focus on active consumers. If system service providers must adapt and become more active short-term providers of system services, then daily system services auctions after day-ahead market awards could also lead to reduced TSO non-energy actions with potential reductions in dispatch balancing costs for consumers.

We also firmly believe that the criterion of "accuracy"⁸ is key and that the TSOs and DSOs should, with the support of the MMU, provide an estimate on the volumes needed for the existing 14 defined system services ideally on an annual basis from 2023-2030. The product volumes estimate would ideally include a view on the shortage of products and locations. This knowledge would greatly help the RAs in our view to make an early informed decision as to the scope of work involved under these new arrangements and to make a timely decision as to the appropriate timeline to introduce auctions into system services arrangements which we believe should be May 2023. Please see point 1 in our cover letter for additional insights.

⁷ Energy, capacity, system services

⁸ "The volume of services procured should match the requirements of the system as accurately as possible"

4) Is the general approach to the Project appropriate and complete?

BGE welcomes this scoping paper and the well-organised webinars which provided helpful additional insights on the issues. We do however believe that the immediate next step should be the TSOs/ DSOs' determination of volumes and related dates of need as outlined in point 1 of our cover letter and in answer 3 above. This will go a significant way to informing the RAs on how quickly a move to daily auctions can and should be accommodated. Where volumes required are likely to exceed offers for example a move to daily auctions by 1 May 2023 should be readily achievable. As referenced in our cover letter also a view in early 2021 on the timeline for adopting auctions and related milestones to achieve the timeline should ideally be published to enable investment decisions. We believe that a short separate consultation on terms of reference for the system services arrangements project could also be useful and that there are learnings from the I-SEM project e.g. the establishment of a Rules Liaison Group, independent certification of systems that could be applied to this project also.

5) For which products is a market-based approach appropriate? What sort of market-based approach is most appropriate?

6) For which products is a market-based approach not appropriate? Why is a market-based approach not appropriate for these products? Will an alternative approach be more economically efficient? What sort of alternative approach should be considered?

BGE answers both questions 5 and 6 together.

We believe that the starting point should be that a market-based approach is appropriate for all system services.

Auction-based procurement on a system wide basis should be possible for both frequency-based and non-frequency-based system services. It is not straight-forward or appropriate to simply decide that for example non-frequency services such as voltage and inertia are not suitable for system-wide auctions. Inertia for example is a system wide issue and could be procured in system wide auctions. A decision not to use a system-wide auction for procuring a system service should be informed by the TSO/ DSO analysis we request in point 1 of our cover letter. TSO analysis should demonstrate if an auction may undermine security of supply or cost-effective outcomes. BGE is not in favour of bilateral contracts for any system service primarily as they counter the consumer value criterion and greatly undermine competition. Where the TSO/ DSO can evidence the extent of a local system service problem and any limits on competition that could undermine outcomes that deliver value for the consumer, alternative solutions should be considered in parallel to considering alternative competitive procurement of the system service(s). Taking the Greater Dublin area for example, our understanding from the Locational Scarcity Scalars papers is that the Dublin constraints issue (which as we understand it limits the breadth of market participants that can contribute to alleviating Dublin's voltage issues) will be resolved by 2027. In the meantime, grid solutions such as the installation of static devices can help the issue together with the planned reinforcements for Dublin to alleviate constraints. BGE is not in favour of additional system service-related payments (beyond the existing locational scalars) benefitting only units that are based in Dublin. Any solution adopted under the future arrangements to ensure security of supply in Dublin at least cost for the consumer, should a) first consider how market participants both inside and outside Dublin can competitively contribute to the solution; and b) be designed in a manner that does not negatively commercially impact units based outside Dublin (which impact is a real probability due to the payment basis of the current locational scarcity scalar for 4 of the 6 system services).

Please see Point 2 of our cover letter and our answer to question 16 below regarding appropriate regulatory intervention and consumer protection.

7) Do stakeholders believe the current qualification process, is the most efficient approach? Do stakeholders have any alternative proposals?

BGE believes that there are significant issues with the current qualification process particularly when it comes to DSUs. The current timeline for completion of registration and testing of a DSU is ~125 working days (or 6 months). The same timeline would apply for a second DSU if the first DSU application has not been completed. If the first DSU's application has been completed (e.g. if one decided to wait for it to complete) the timeline for registering and testing second and subsequent DSU units is ~60 working days. These timelines are in our view unduly long and unacceptable. It is a barrier to entry in a timely manner and restricts competition and opportunities for the TSO to benefit from improved system services. The requirement for a DSU operator to have signed contracts with each constituent demand site before beginning registration is also removed from commercial reality and acts as a serious disincentive for DSU operators and demand site owners to participate in the market. BGE also believes that

requiring individual demand sites that have qualified under one DSU to re-test again if it seeks to move to another DSU (which DSU itself has already qualified) is inefficient and should not be required. Given the expected growth in demand side response, including large demand from data centres, it is imperative that these issues are addressed in the very near term. A level playing field between existing and prospective system services providers should exist. We have suggested an incentive in our response to the CRU on PR5 with the above context in mind such is its importance in opening up the market.

BGE also believes that the Qualification Trial Process (QTP) is inhibited in enabling the qualification of DSUs due to the definition of a DSU under the SEM Trading & Settlement Code (T&SC).⁹ The cap of 10MW MEC of the size of the individual customer demand sites behind the DSU inhibits the development of DSUs by limiting their size and economies of scale, thus curtailing their ability to mitigate risk. We request that steps are taken to remove this limit and we would welcome further discussion in this regard. Market experience has shown that likely future contributors to the demand side response (DSR) space may breach the 10MW limit. The 10MW limit stifles the potential contribution of DSR to energy, system services and capacity markets. We consider it a 'regulatory distortion' contrary to the objectives of EU legislation.¹⁰ Finally on this issue BGE has experienced difficulties with ensuring maximisation of the benefits in terms of system services that a DSU can offer due to assets being limited to only having a head-meter, as opposed to sub-meters being permitted, on a site. Enabling sites to have sub-metering would greatly increase the system service offering potential of DSUs. BGE would welcome further discussion on this point.

The current 6-monthly windows for tender are adequate in the context of the current regulated arrangements.¹¹ Our understanding is that going forward, if daily auctions are adopted that the qualification requirement would be a one-off test and once registered, a unit is effectively granted a "lifetime" contract. Then the unit's capability to offer and delivery of system services is updated daily. Should the unit find itself in a position that it can provide more volumes of a system service(s) than it originally qualified for then updates of these contractual capabilities should be permitted as regularly as possible on an ad-hoc basis with as short approval timelines as possible.

8) What are stakeholder views on the overall current governance arrangements including the contractual principles, the Protocol Document and the market ruleset? Should these be modified into an overall protocol document which captures all of the rules for providing and procuring System Services with increased regulatory oversight?

Yes, we believe that governance of these arrangements should rest primarily with the RAs. Consideration should be given to amalgamating documents into an energy market Trading & Settlement Code type approach. We also request clarification as to the continued application of the current market ruleset whereby the payment basis for certain products is linked to either ex ante positions or physical dispatch position. Is it envisaged that the market ruleset will be revised and if so at what point will this be revised?

9) Should System Services continue to be funded through network tariffs? Are there views on any alternative arrangements?

Yes, we believe that system services should continue being funded through network tariffs. We have not seen alternative evidence that another approach would be beneficial for consumers. We note that the UK continues to recover system services costs via transmission charges. Our view is that by putting the cost on suppliers directly on a weekly basis would undermine the transparency and ease of monitoring of the DS3 payments that are made by the TSO. Putting the costs through suppliers on bills could also dilute the TSOs' role in managing DS3 services and keeping costs as low as possible for consumers. Suppliers are also less well-placed than the TSO to forecast system services costs and suppliers would have difficulty in accurately forecasting this cost for customer price predictability reasons.

We are also in favour of the current publications of annual DS3 spend in Ireland and Northern Ireland continuing in the new arrangements.

⁹ Section B.9.5 of the T&SC

¹⁰ E.g. article 20 EU Electricity Regulation (EU) 2019/943

¹¹ Please however see our response to EirGrid's DS3 Mitigation of Service Provider Financial Risks due to COVID-19 consultation whereby we support Option A (more regular tender windows in 2021)

10) Should all services be procured through a single daily auction framework or should bespoke arrangements be developed for the separate products?

In general, when there are products for which an auction approach is determined as suitable, then the same auction format should apply across all of these products, i.e. one auction design such as a demand curve which sets a clearing price relative to volumes on the system should apply no matter what the product is. Constraints should not influence the clearing price – a single clearing price per product/ bundle should apply. We believe that this principle of the same auction format design and operation applying to all products, can apply regardless of whether some products are “bundled” (e.g. reserves products) for auctions or not.

Where system wide auctions put securing the required volumes of a system service(s) at risk such that either security of supply or efficient cost-effective procurement is undermined, this must be robustly evidenced by the TSO/ DSO in line with our request for insights on volumes needed for 2023-2030 under point 1 in our cover letter above. BGE is not in favour of bilateral contracts for any system service – competitive procurement options must be assessed exhaustively in the first instance.

Considering decarbonisation targets we believe that, based on evidence from the TSOs/DSOs of volumes of products required by particular dates and the existence of service providers to provide such products, consideration of longer-term contracts for certain developing technology types may be merited. It is necessary however that strict criteria apply in that these long-term contracts are allocated only to new technologies that prove their main focus is grid support services and that they are reliant on system service revenue for a specified high percentage of overall revenues. BGE is not however in favour of offering long term contracts due to a lack of sufficient competition in an area.

11) What are stakeholders' views on the timing of auctions?

BGE supports a move to daily auctions for as many system services products as possible. Ultimately, we believe that the RAs should seek to align with the EU legislative requirements as quickly as possible and a move to daily auctions from 1 May 2023 merits consideration.

The procurement of system services should remain separate to the ex-ante and balancing energy markets. Provision of System Services should not determine how a market participant should operate in the energy market; a market participant should reflect its capability to provide System Services based on how they intend to run in the Energy market. BGE favours a solution that sees market-based procurement of system services occurring after day-ahead market results are known. Procuring system services in this manner for example would allow an informed view of reserve requirements given that the largest single infeed, known on DAM results, informs reserve levels. This in turn would help ensure the appropriate level of reserves is procured to deliver value for consumers. If daily auctions with one-day contracts were adopted a potential increase in intraday market liquidity may also be seen whereby market participants buy and sell more volumes in a bid to account for their system service commitments. Procuring system services where market participants have energy market results is also closest to what we have today which could be conducive to a smooth transition to auction-based arrangements. Furthermore, given the current SEM pricing and settlement issues we are experiencing we do not believe there is any merit in considering co-optimisation of system services with the balancing market.

12) Do stakeholders have any proposals on how best to ensure commitment obligations are met?

BGE understands that the current performance incentive applied to the regulated arrangements has a role to play in ensuring the meeting of commitment obligations. Should performance scalars persist in the new arrangements however we believe that the duration for recovery of payments under scalars should be revised to better reflect the value of the service being provided. Our experience shows that notwithstanding the provision of volumes during scalar recovery periods, providing units are penalised for an excessive amount of time. For example, where an engineering fix is carried out to a unit which improves its service provision in terms of outturn volumes, recognition of this improvement can take up to 6 months to feed through in DS3 revenues. The value of units is therefore not being fairly reflected in remuneration which undermines project revenues and business cases.

13) What are the significant interactions within potential System Services product markets and between Systems Services markets and the energy and capacity markets? How should issues arising be addressed?

Regarding interactions within potential System Services product markets BGE believes there is scope to “bundle” certain products for auction procurement e.g. reserves. The technical nature of the provision of primary operating

reserve (POR) for example is linked to the incidental provision of other reserve products which provide valuable service to the TSO/ DSO and consumers. Compatibility of products and bidding rules where applicable is necessary before bundling. The choice of which products to bundle or not should be done bearing in mind that the optimisation function that will apply in the procurement method is transparent, predictable and allow market participants to replicate and validate outcomes. Such validation could for example be undermined where products are bundled with other products to which different market power controls may apply. BGE is not in favour of solutions that will render pricing and commitment outcomes unverifiable or unpredictable.

Regarding the interaction between the system services markets and the energy market, please see our answer to question 11 above for our view on the timing of system services auctions. Ultimately system service provision should not determine how a market participant should operate in the energy market; a market participant should reflect its capability to provide System Services based on how they intend to run in the Energy market. Auctions after day-ahead market results would help inform the level of reserve required to deliver best value for consumers. Daily auctions could also see an increase in intraday liquidity and the timing is closest to what we have today which should be conducive to a smooth transition to new arrangements. Given the ongoing SEM pricing and settlement issues we are experiencing we do not believe there is any merit in considering co-optimisation of system services with the balancing market. Such co-optimisation could also in our view result in a lack of transparency, predictability and ability to replicate / validate pricing and auction outcomes.

For many investors capacity and system services revenues (alongside energy revenues) are important for business cases. To facilitate existing and new investors making informed decisions on business cases, a decision on the timeline for changing to the new auction procurement approach would ideally be published by Q1 2021.

14) Do stakeholders have further views or proposals in relation to auction design?

In general, when there are products for which an auction approach is determined as suitable, then the same auction format should apply across all of these products, i.e. one auction design such as a demand curve which sets a clearing price relative to volumes on the system, should apply no matter what the product is. Constraints should not influence the clearing price – a single clearing price per product/ bundle should apply. We believe that this principle of the same auction format design and operation applying to all products, can apply regardless of whether some products are “bundled” (e.g. reserves products) for auctions or not. A uniform auction format would best achieve the “simplicity” criterion proposed for this process.

BGE requests that a project timeline is issued in Q1 2021 outlining the detailed consultation process that will apply in ensuring a move to cost-effective and efficient auction procurement is achieved. We have outlined in our cover letter suggestions around progression of the project building on some lessons from the I-SEM project. The detailed consultation process, informed by the TSO analysis on product volumes outlined in point 1 of our cover letter, should facilitate robust engagement with industry on auction design principles and format that work for all products and deliver competitive costs for services that are as low as possible for consumers. We outline our views on potential market power mitigation needs in our answer to question 17 below.

15) Do stakeholders believe there would be benefit in maintaining the Fixed Contract Arrangements for future procurement runs?

Considering decarbonisation targets we believe that, again based on evidence from the TSOs/DSOs of volumes of products required by particular dates and the existence of service providers to provide such products, consideration of longer-term contracts for certain developing technology types may be merited. It is necessary however that strict criteria apply in that these long-term contracts are allocated only to new technologies that prove their main focus is grid support services and that they are reliant on system service revenue for a specified high percentage of overall revenues. BGE is not however in favour of offering long term contracts due to a lack of sufficient competition in an area – long term contracts would lock consumers into paying for higher priced system services on a long-term basis stifling the potential growth of competition in the system service(s).

16) Do stakeholders have views on the list of additional considerations above? Are there any further issues to consider?

We address the potential issues of market power point in our answer to question 17 below.

Regarding providing sufficient investment certainty for viable projects to be progressed which facilitate the energy transition, we believe that a move to daily auctions in May 2023 (with preceding auction trials) will greatly facilitate the take up in low carbon technologies such as DSUs and batteries. An early decision on the timeline for the move to daily auctions would help investment planning in this regard. We believe that existing system service providers will need to adapt but that the change required is not insurmountable and we note that these auctions are already in operation with great success in mainland Europe. Achieving the change should ultimately lead to competitive cost outcomes providing system services at the lowest cost for the consumer in line with the EU's aims around decarbonisation. There is potential too that procuring system services after the day-ahead market could reduce TSO non-energy actions with consequential possible reductions in dispatch balancing costs for consumers.

As outlined in point 1 of our cover letter we believe that the TSOs/DSOs together with the MMU should provide a report as soon as possible on the volumes of system services required from 2023-2030. The TSO/DSO analysis would ideally include a view on the shortage of products and locations of shortages. This would help inform the capability of moving to auctions by May 2023 which we believe is feasible for many of the system services in question. Without any robust evidence of barriers or major drawbacks to auction implementation we do not believe that significant (if any) mechanisms to smooth the transition from regulated contracts to competitive auctions are required.

17) What are stakeholders' views on the potential existence of, and options for mitigation of, market power?

While on the face of it some system service products may have an obvious market power issue, we believe that the default starting design position should be that no price caps or bidding rules are necessary for products/ product bundles until the potential for market power abuse to the detriment of competition and the consumer is robustly evidenced. This evidence of potential to exercise market power abuse can be informed by the TSO/DSO analysis we request in point 1 of our cover letter. The evidence used to inform the extent of any regulatory intervention could for example include determination of (a) the volumes of the 14 products required at certain points in time, (b) the locations in which these products are required, (c) the number of market participants in a position to offer these products in these locations, (d) whether the products are for the transmission and/ or distribution system. BGE supports regulatory intervention where the need for such is robustly evidenced and with the above suggested list of information, we believe the RAs can make informed decisions that ensure competition puts pressure on prices for the benefit of consumers. Where there is a strong risk that competitive pressures will not exist then appropriate, targeted (and of limited duration) intervention could apply.