

SEM-19-003
Framework for NEMO Regulation from October 2019

Response to Consultation Paper

by

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CONTENTS

1	Executive Summary.....	3
2	Consultation Question 1.....	5
2.1	Response	5
3	Consultation Question 2.....	6
3.1	Response	6
4	Consultation Question 3.....	7
4.1	Response	7
5	Consultation Question 4.....	8
5.1	Response	8
6	Consultation Question 5.....	9
6.1	Response	9

1 EXECUTIVE SUMMARY

SONI Ltd and EirGrid plc as designated Nominated Electricity Market Operators (**NEMOs**) for Northern Ireland and Ireland respectively (hereafter **SONI and EirGrid**), welcome the opportunity to respond to the Framework for NEMO Regulation from October 2019 consultation, SEM-19-003, (the '**Consultation Paper**') as issued by the Commission for Regulation of Utilities and the Utility Regulator (the '**Regulatory Authorities**', '**RAs**') on the 28th January 2019.

In 2015, SONI applied and was designated¹ as a NEMO in Northern Ireland and EirGrid applied and was designated² as a NEMO in Ireland, by the Utility Regulator and the Commission for Regulation of Utilities respectively, for operation of the single day-ahead markets within the framework of the Commission Regulation 2015/1222 on establishing a guideline on capacity allocation and congestion management ('**CACM**').

SONI and EirGrid work together, through a Contractual Joint Venture, SEMOpx, to jointly deliver NEMO services including; registration of market participants, market systems operation (excluding the operation of EUPHEMIA), settlement, credit risk management, managing currency risk, and providing access to market data for the all island SEM Market.

SONI and EirGrid, though SEMOpx, also operate the intraday coupling arrangements in the SEM.

With regard to Brexit, it is clear that the outcome for the SEM in terms of potential changes, amendments, and challenges depends largely on whether an agreement is reached between the European Union and the United Kingdom whereby Union law and CACM under Article 1(4) could be applied at least in Northern Ireland. Given that there is a level of ambiguity as to the underpinning governance structure of any Brexit, EirGrid and SONI have provided the response below subject to a number of caveats.

Article 1(4) of CACM provides for the delivery of NEMO services outside of the European Union but only by agreement with the European Union and where it is clear that CACM would apply where such NEMO services are being delivered.

From the withdrawal date, SONI could therefore potentially no longer be validly designated as a NEMO. This has implications for participants based in Northern Ireland and for SEMOpx.

EirGrid is designated as a NEMO to provide NEMO services in Ireland only. While EirGrid could potentially passport as a NEMO to another Member State or part of a Member State; arguably, EirGrid could only do this in a third country where there was an appropriate agreement in place between that third country (the United Kingdom) and the European Union. Our current

¹ Decision on NEMO Designation for Northern Ireland ([here](#)) & Designation Order ([here](#))

² Decision on NEMO Designation for Ireland ([CER/15/237](#)) & Designation Order ([CER/15/239](#))

understanding is that the UK authorities intend to revoke (and not transpose) CACM and FCA in the event of a hard Brexit.

Subject to the above and to any broader agreement between the UK and the EU, in order for SONI to provide NEMO services post-Brexit, some additional regulatory requirements may be imposed and these obligations would have to be put in place and complied with.

This is a separate sovereign matter for both the European Union and United Kingdom and issues which flow from those negotiations, potentially impacting the SEM would have to be considered by impacted parties separately when any deal is struck or has definitively failed to have been agreed, and when the terms of any Brexit become apparent.

SONI and EirGrid have based their response to the Consultation Paper on the assumption that there is continued alignment of the day-ahead and intraday market regulatory framework in Northern Ireland and Ireland.

SONI and EirGrid are broadly supportive of the RAs' preferred regulatory framework approach in terms of having:

- i. A 3-year fixed duration for designation from 3 October 2019; and
- ii. Where SONI and EirGrid are re-designated as NEMOs that an allowed revenue model, inclusive of an appropriate remuneration framework, be applied for the duration of the designation period; and
- iii. That the associated tariffing and fee structure are suitably flexible in the event of another NEMO entering the market.
- iv. Consideration of a transition to a competition based regulatory model at the end of the fixed duration period, if competition has occurred.

SONI and EirGrid see the above approach as a balanced approach to maintaining the efficient and effective operation of the key SEM day-ahead and intraday markets, while considering the commercial realities of NEMOs and also allowing the opportunity for competition to evolve in line with CACM requirements.

SONI and EirGrid note the proposed deadline for the submission of applications to be designated as NEMOs by competent authorities in SEM as being 5 April 2019 for a designation period from 3 October 2019; and will consider the proposals outlined in this Consultation Paper as part any respective NEMO re-designation applications.

2 CONSULTATION QUESTION 1

Consultation Question 1: The RAS invite feedback on whether the next term of designation should be time limited and for how long.

Option 1: The RAs are considering whether the next term of designation (from October 2019) will apply on an enduring basis. If this option is put in place, a process for any designated NEMO to terminate its designation would need to be developed.

Option 2: A time-limited designation could be applied from October 2019. At the end of this period the designation NEMO would have the option to re-apply for the next term of designation. This is currently the RAs' preferred option as it would provide certainty to market participants for this period and could align with the application of a price control. A period of three years is proposed by the RAs for designation from October 2019.

It is proposed that applications for designation from interested parties will be accepted until 5 April 2019.

2.1 RESPONSE

Option 1 which provides for designation on an enduring basis would, under the current regulatory framework in Ireland and Northern Ireland, particularly as applied to EirGrid and SONI in regard to the licence conditions as currently extant in the respective Market Operator Licence, be of notable concern in the absence of a clearly defined process for a NEMO to be able to terminate its designation. No arrangement should be such that it seeks to bind a party to provide services for an extended period of time where it is not commercially prudent for the party to do so.

Option 2 which provides a fixed term for designation of three years from October 2019 seems prudent, but only where such an approach is applied in combination with an appropriate regulatory revenue framework and/or the necessary arrangements are in place to enable a NEMO to terminate its designation.

Option 2 in combination with an appropriate regulatory revenue framework strikes the balance of providing some certainty to SEM participants in the medium term; while ensuring that EirGrid and SONI (if re-designated) are not locked into obligations for an extended period of time that could be commercially difficult to maintain.

EirGrid and SONI therefore support Option 2, of a three year period of designation, if applied in combination with an appropriate regulatory revenue framework.

3 CONSULTATION QUESTION 2

Consultation Question 2:

Option 1: In the event that SEMOpx successfully applies for re-designation and no other NEMO is operational at that point in time, it is proposed that a price control would apply to SEMOpx from October 2019. Such a revenue control would apply for an interim period of three years regardless of whether another NEMO enters the SEM and competition arises in the market during this time. This is the RAs' preferred option at present.

Option 2: Should SEMOpx successfully re-apply for designation, a revenue control could apply for an interim period of three years. However, if more than one NEMO entered the market and reached a certain threshold of market share, revenue regulation would cease.

Option 3: Alternatively, a price control could cease to apply to SEMOpx at the end of the initial designation period, with SEMOpx setting its own fees if designated. If more than one NEMO enters the market on this basis, fees could be adjusted based on competitive pressures.

Responses from interested stakeholders are invited on this proposal.

3.1 RESPONSE

In determining the revenue regulation and timeframes for its application, EirGrid and SONI note the importance of seeking to balance a number of potentially competing elements. Namely ensuring:

- a. a level playing field for any NEMO operating in the SEM - whether existing or new.
- b. adequate availability of NEMO services, for all SEM participants
- c. NEMOs maintain NEMO service obligations while allowing for commercial realities

EirGrid and SONI believe that Option 1 is a workable option in the event that SONI and EirGrid are re-designated as NEMOs and no other NEMO enters the SEM, subject to any such revenue control providing an appropriate allowed revenue model, inclusive of a remuneration framework – specifically it is important it represents a revenue not a price control. Aligning such a revenue control to the designation period provides security to the SEM Participants that a NEMO with regulated revenues would be in place in medium term. Such an approach would however need to consider the arrangements pertaining to the associated tariffing and fee structures to ensure they are suitably flexible in the event of another NEMO entering the market.

EirGrid and SONI do not support Option 2 and do not believe that it fulfils, as currently set out, one of the RAs stated objectives of ensuring a level playing field for any NEMO operating in the SEM. The enablement of Multi NEMO Arrangements in the SEM is not akin to a market opening exercise where RAs sought to revenue/price regulate longstanding incumbent parties to force

the loss of market share. A subjective decision about when competition is sufficient to trigger the change in revenue control is not appropriate and to enable proper consideration of such a proposal would require a clear proposed framework to be set out and consulted on.

Further EirGrid and SONI believe that this approach has the potential to expose the SEM to issues around market access for all participants. Given the nature of the SEM, the day-ahead and intraday markets are the exclusive trading options and it is therefore critical that all participants have access to these markets given the balance responsibility of the SEM design. However, the provision of intraday market services is not a CACM requirement, at present, but is provided to the SEM by EirGrid and SONI through SEMOpx. Implementing a threshold for market share criteria could lead to a situation where not all participants are able to maintain access to day-ahead and intraday markets, should one or more NEMOs then subsequently withdraw its NEMO services, or alternatively target only a specific group of participants.

EirGrid and SONI also see some value in Option 3 which would allow SEMOpx to provide NEMO and intraday services and have commercial independence over its own fees. This would allow market forces to moderate the extent of NEMO services and associated costs to SEM participants. EirGrid and SONI recognise that Option 3 may be of concern to SEM participants as, at least initially, it is likely there will be limited competition in place at the start of the designation period. EirGrid and SONI are of the view that if Option 3 was applied then the corresponding regulation of the NEMOs through EirGrid and SONI Market Operator Licences which currently includes explicit requirements to provide the full range of NEMO services, compliance with the TSC, and approval of SEMOpx Rules, would no longer be appropriate under CACM requirements and European law more generally and would need to be modified.

Based on the options presented, EirGrid and SONI would support Option 1 subject to an appropriate allowed revenue model, inclusive of a remuneration framework, being established and arrangements pertaining to the associated tariffing and fee structures being suitably flexible in the event of another NEMO entering the market.

4 CONSULTATION QUESTION 3

Consultation Question 3:

If a price control continues to apply to SEMOpx (should SEMOpx successfully re-apply for designation), it is proposed that this is applied for a three-year period, linked to a time-limited designation period. Responses from interested stakeholders are invited on this proposal.

4.1 RESPONSE

As outlined in our response to Consultation Question 3, SONI and EirGrid see the value of a three-year revenue control period linked to a time limited designation period. This would provide security to SEM Participants that a NEMO with regulated revenues is in place in the

medium term. For this reason SONI and EirGrid would be supportive of this proposal subject to an appropriate allowed revenue model, inclusive of a remuneration framework, being established and arrangements pertaining to the associated tariffing and fee structures being suitably flexible in the event of another NEMO entering the market.

5 CONSULTATION QUESTION 4

Consultation Question 4:

The RAs are reconsidering the potential revenue model to apply to SEMOpx from October 2019, along with the form of remuneration that should apply to SEMOpx. While this would be considered in more detail as part of the Draft Determination and Final Determination papers for any further price control applied to SEMOpx, comments on the form of remuneration SEMOpx should receive under an allowed revenue approach are invited.

5.1 RESPONSE

The details of the price control regulation for EirGrid and SONI in operation of SEMOpx can be found in SEM-17-096. The current revenue model is based on an allowed revenue approach, with the efficient costs associated with SEMOpx being underwritten. Any over or under recovery of costs will be corrected through a k-factor mechanism, although the details of how this will be applied depend on whether SEMOpx continues to operate at the end of the designation period.

At the time of the first price control, EirGrid and SONI highlighted the need for SEMOpx, as an Asset Light business, to have in place an appropriate regulatory revenue framework.

The RAs in the Consultation Paper recognise that should a price control apply from 3 October 2019, consideration will need to be given to remuneration to apply to SEMOpx that is consistent with remuneration provided from other parts of the licensees' activities as Market Operator.

EirGrid and SONI welcome the RAs' proposed approach.

6 CONSULTATION QUESTION 5

Consultation Question 5:

Consultation Question 1 indicated the RAs' preferred approach of applying designation from October 2019 on a time-limited basis, while Consultation Question 2 set out the RAs' preferred option whereby a revenue control, if applied to SEMOpx, would apply for an interim period of three years regardless of whether another NEMO enters the SEM and competition arises in the market during this time.

The RAs' preferred approach regarding Consultation Questions 1 and 2 will need to be considered in the context of this final proposal [a transition to a competition based regulatory model] , as previous proposal as discussed in the Consultations Paper are summarised together here in a proposed overall approach.

Based on this, feedback is requested from interested stakeholders on the overall proposal to apply revenue regulation to SEMOpx from October 2019 for a three-year period, should SEMOpx successfully apply for re-designation. It is further proposed that revenue regulation will continue to apply to SEMOpx from October 2019 for a three-year period, to be aligned to a designation period of three years. The RAs' final proposal is that these arrangements would not change regardless of whether another NEMO enters the market during this three-year period or not.

6.1 RESPONSE

EirGrid and SONI are of the view that there are a number of key issues which should be considered and reflected in the final proposed approach:

- a. The need to provide certainty to SEM participants in an environment that access to the day-ahead and intraday markets will be provided, noting in particular that intraday auction services are not currently a prescribed NEMO activity under CACM.
- b. The need to provide clarity to EirGrid and SONI, in so far as their designation status is captured under licence conditions with the Market Operator Licences, a clear process by which it can seek termination of its designation, where an appropriate price control/revenue control arrangement is not also in place.
- c. The need for a level playing field between NEMOs when or if other NEMOs become active in the SEM. In this regard the proposals as set out in Section 7 of the Consultation Paper in terms of licence obligations where a NEMO other than SEMOpx is designated or an additional NEMO seeks to operate in the SEM would not be subject to licence conditions may need to be revisited.
- d. The need to ensure that any regulation of any NEMO should be fair and reasonable, proportionate and CACM compliant.