

TSO CERTIFICATION NORTHERN IRELAND

Decision Paper

SEM-11-103

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1. Background

The Gas and Electricity (Internal Markets) Regulations (Northern Ireland) 2011, which amends the Electricity (Northern Ireland) Order (1992), requires that a person who participates in the transmission of electricity, and who holds a transmission licence immediately before the coming into operation of the 2011 Regulations, must on and after the relevant date, ensure that he is certified at all times when he acts under the authority of that licence. These requirements transpose into Northern Ireland law the obligations of Directive 2009/72/EC of the European Parliament and of the Council of 13 July 2009. The purpose of this notice is to invite application for certification and advise on the information to be submitted to assess the application.

The amended Order includes identification of the participants in transmission that require to be certified in Article 10B (1) and (2) and the grounds for certification in Article 10F. For the purposes of Article 10B a person must ensure that he is certified if he holds a transmission licence at the relevant time and participates in the transmission of electricity within the meaning of (b) or both (a) and (b) of Article 8(4) of the Order reprinted below —

“(a) he co-ordinates, and directs, the flow of electricity onto and over a transmission system by means of which the transmission of electricity takes place; or

(b) he makes available for use for the purposes of such a transmission system anything which forms part of it.”

The requirement for certification therefore applies to electricity transmission and electricity interconnectors. The applicant has eight weeks from the issue of this notice to submit an application for certification.

The SEM Committee of the Utility Regulator decided in May 2011 that the issue of TSO certification for Northern Ireland was a ‘SEM matter’. Consequently, decisions as to the exercise of the Utility Regulator’s functions in relation to this issue are being taken on its behalf by its SEM Committee. References to the Utility Regulator in this document should be read in that context.

The guidance provided in this document reflects the views of the Utility Regulator as at 5 December 2011. It should not be taken as indicative of the views of any other body, including the Department of Enterprise Trade and Investment and the European Commission, as to the matters discussed. This document is also subject to revision in order to take into account developments following 5 December including any decisions

taken, or any opinions or guidance provided, by other bodies such as the Commission or the courts

2. Grounds for Certification

Article 10F provides four grounds for certification: ownership unbundling, derogation from ownership unbundling on the grounds in paragraph (9) of Article 9 of the Directive; derogation from ownership unbundling on the grounds of nomination of an Independent System Operator, and having been granted an exemption under Article 17 of the Electricity Regulation (new interconnectors).

Article 10G sets out the requirements of the first certification ground in Article 10F (3). Commission Staff Working Paper SEC(2011) 1095 final provides practical guidance on how the Commission will treat and assess notifications by National Regulatory Authorities of preliminary decisions and information necessary for its assessment of the decisions.

The second ground for certification in Article 10F (4) “is that the applicant has applied for a derogation from the ownership unbundling requirement on the grounds in paragraph (9) of Article 9 of the Directive (alternative arrangements for independence)”. This provides for certification “where, on 3 September 2009, the transmission system belongs to a vertically integrated undertaking and there are arrangements in place which guarantee more effective independence of the transmission system operator than the provisions of Chapter V” of the Directive.

The third ground for certification is set out in Article 10F (5) of the Regulations. Articles 13 and 14 of the Directive contain specific requirements which must be met in order to satisfy this ground for certification.

Applicants should set out the grounds for their application with reference to the circumstances that warrant the application. If not applying under the first certification ground of full ownership unbundling set out in Articles 10F (3) and 10G of the Regulations, applicants should explain why they are not eligible on this ground. Where the applicant is not making an application on the grounds of full ownership unbundling the Regulations allow application under the Independent System Operator model and under paragraph (9) of Article 9 of the Directive. Applicants should set out their eligibility for the particular grounds chosen for their application.

Those considering submitting applications for certification on the basis of either the second or third grounds for certification should note that the SEM Committee considers

that (having regard to the purpose of the Directive, as reflected in particular in recital (16) of the preamble) these grounds may be available only in respect of a transmission system which remains within the ownership of the same vertically integrated undertaking which owned it on 3 September 2009.

3. Procedure for Certification – General

The EC Staff Working Paper provides questionnaires which describe the information, including general information, necessary for its assessment of the preliminary decisions of the certification procedure for Ownership Unbundling, Independent System Operator and Independent Transmission Operator models. It does not provide specific guidance on the information requirements of an application on the second ground of the Regulations.

The second ground, allowing for a derogation from the ownership unbundling requirement for the purpose set out in recital (16) of the Directive, provides for certification in the event that, on 3 September 2009, the transmission system belongs to a vertically integrated undertaking and there are arrangements in place which guarantee more effective independence of the TSO than the provisions of Chapter V of the Directive. The format and content of the ITO checklist set out in EC Staff Working Paper SEC(2011) 1095, in addition to the purpose and requirements set out in recital (16) and Chapter V of the Directive, are therefore useful cross-checks for the purposes of the evidentiary requirements for an application for derogation on the grounds in paragraph (9) of Article 9 of the Directive. Where the applicant is not able to meet any individual requirement of the ITO checklist and Directive, it would be expected that the applicant would provide evidence showing that the arrangements in place are nonetheless such as to guarantee more effective independence of the TSO.

In undertaking the task of assessing applications under Article 9(9) regard will be taken not only to the provisions of Article 9(9) and Chapter V but also to the surrounding context as articulated in the preamble to the Directive (and in particular recitals (11), (12), (16) and (19)) and also the Commission's own Staff Working Paper on The Unbundling Regime dated 22 January 2010. Extracts from these recitals plus additional notes are contained in Appendix 1.

4. Procedure for Certification – Article 9(9) Derogation

The arrangements in place at 3 September 2009 are subject to test and the applicant must submit evidence for those arrangements. However it will also be necessary for the applicant to address any significant or material changes to these arrangements since that date. This will require full description of changes, their impact on the eligibility for the Article 9(9) derogation taking account of its stated purpose, the grounds for certification and full and complete provision of evidence of these changed arrangements. The onus is on the applicant to demonstrate eligibility in the circumstances as they exist.

An assessment of the effectiveness of Article 9(9) arrangements (and the relative effectiveness of those arrangements as compared with the provisions of Chapter V of the Directive) should be principally concerned with the following areas, address the following questions and provide evidence that may include, but not be limited to, the following:

1. Resources: Does the applicant have the necessary human, technical, financial and physical resources to carry out its tasks and functions?

Evidence may include a description of tasks as set out by Articles 12 and 22 of the Directive; description of human resources including terms and conditions of employment; organisation chart; unbundled accounts; asset register; certification of ownership of assets, and descriptions of technical and physical resources.

2. Organisation, Governance and Incentives: How effective are the arrangements in ensuring that TSO functions are performed independently of any vertically integrated undertaking concerned? How effective are the arrangements in removing the incentive for the vertically integrated undertaking concerned to discriminate against competitors as regards network access and investment?

Evidence may include a Group Chart of the applicant within the vertically integrated undertaking (VIU) showing shareholdings and activities; membership, powers, governance documentation and minutes of the Supervisory Body; Compliance Plan and the identity, job description and employment conditions of the Compliance Officer; copies of standard procurement and tendering procedures/policies/contract terms; certification of separation of IT systems etc.; description of the communication strategy, corporate identity, branding and premises, and details of auditors to the applicant and VIU.

3. Information: How effective are the arrangements in preventing the vertically integrated undertaking concerned obtaining access to information relating to the performance of TSO functions?

Evidence may include corporate policies and procedures and contracts of employment.

4. Regulation: How effective are the arrangements in terms of producing a regulatory regime which is transparent and efficient and not overly onerous for the National Regulatory Authority?

Evidence may include description of the arrangements for compliance and how these may fulfil the requirements to be transparent and not overly onerous for the National Regulatory Authority.

In reaching a decision on relative effectiveness consideration will be given to the overall effects achieved by the arrangements in question and not simply the individual effects of each of the matters highlighted above. The onus is on the applicant to demonstrate that there is more effective independence guaranteed by the arrangements in question.

The questions are therefore indicative of those that might be addressed and provide only examples of the evidence that might be provided to substantiate responses. The applicant may also wish to address questions arising from the Independent System Operator model in its demonstration of the effective independence of the overall arrangements pertaining to transmission system operation in Northern Ireland. These questions and those relevant to the other grounds for certification are contained in the Commission Staff Working Paper SEC(2011) 1095 final.

In particular the applicant should fully describe the arrangements in place governing the operation of the Transmission System and the roles of related transmission licensees. It should therefore consult with all related licensees so that it can fully evidence the respective roles, tasks and responsibilities of those involved in electricity transmission.

Applications should contain sufficient information and analysis to enable a complete understanding of the arrangements, be contained within a single document and allow an informed decision to be made without reference to any other information or documentation. The applicant should therefore consider provision of all information relevant to the grounds for certification without limit to that specifically required by the questions raised in the Directive, Commission Staff Working Paper or those above. The information should nevertheless be suitably focussed on the relevant issues.

The applicant should clearly identify any information in the application which is considered to be confidential and for each piece of information identified provide an explanation as to why that information is confidential. The application should be

authorised by an appropriate Director confirming that the documentation contained is true and complete and that any event or circumstance which may affect the basis of certification will be notified to the Utility Regulator.

This guidance is not a substitute for the requirements of the Directive or the Order as amended. The Utility Regulator reserves the right to request additional information or clarification as per Article 10C (7) of the Electricity Order (1992) as amended.

5. Process for Certification

The Directive, amended Order and Commission Staff Working Paper set out (or authorise the Utility Regulator to determine) the process, including timescale, to be followed in assessment of an application:

- Applications must be made in writing within eight weeks of publication of this guidance dated 5 December 2011 and should address the issues raised in this Guidance, the amended Order, Directive and Working Paper and contain the information required as evidence to support certification. The closing date for applications is therefore 30 January 2012.
- The applicant is obliged under Article 10C(1) of the amended Order to consult with related transmission licensees in respect of the application before it is submitted to the Utility Regulator. Consultation shall be in writing allowing the related licensees no less than two weeks within which to submit comments in response to such consultation.
- The applicant is obliged under Article 10C(3) of the amended Order to send a copy of its application to any related transmission licensees at the same time as it is submitted to the Utility Regulator. Should any such party wish to make representations to the Utility Regulator in respect of any application copied to it, these must be submitted in writing within 21 days of receipt of such copy application.
- A related licensee may make such representations on the application for certification as it thinks fit to the Utility Regulator, which shall have regard to any representations made and what, if any, qualification measures should be taken. Such representations must be made within 21 days of receipt of the application.
- The Utility Regulator may request any further information (from an applicant, a related transmission licensee, a relevant producer or supplier) as it considers

relevant to the application and that information must be supplied if it is either, in their possession or control, or if it could reasonably be expected to obtain it. Such information must be provided by the date specified in the request.

- The Utility Regulator will, within four months beginning with the day on which it receives an application for certification, make a preliminary decision as to whether it should certify the applicant. This period may be extended if further information has been requested and not supplied by the date specified. The period may be extended by the amount of the delay.
- After making the preliminary decision the Utility Regulator shall notify the applicant, related transmission licensee, the Department and the European Commission.
- The Commission has two months in which to examine the decision and deliver its opinion. The Commission may also request the European Agency for the Cooperation of Energy Regulators (ACER) to provide its opinion of the decision, in which case the period may be extended by a further two months.
- Within two months of receiving the opinion of the Commission the Utility Regulator shall adopt a final decision regarding certification taking the utmost account of the opinion of the European Commission. In the absence of an opinion the Commission shall be deemed not have raised objection to the preliminary decision.
- Where an application for derogation on the grounds in paragraph (9) of Article 9 of the Directive has been made the European Commission, rather than the Utility Regulator, will take the final decision.

Appendix 1

- Recital (11) notes that, "Only the removal of the incentive for vertically integrated undertakings to discriminate against competitors as regards network access and investment can ensure effective unbundling. Ownership unbundling, which implies the appointment of the network owner as the system operator and its independence from any supply and production interests, is clearly an effective and stable way to solve the inherent conflict of interests and to ensure security of supply. For that reason, the European Parliament, in its resolution of 10 July 2007 on prospects for the internal gas and electricity market [...] referred to ownership unbundling at transmission level as the most effective tool by which to promote investments in infrastructure in a non-discriminatory way, fair access to the network for new entrants and transparency in the market";
- According to recital (12), "Any system for unbundling should be effective in removing any conflict of interests between producers, suppliers and transmission system operators, in order to create incentives for the necessary investments and guarantee the access of new market entrants under a transparent and efficient regulatory regime and should not create an overly onerous regulatory regime for national regulatory authorities";
- Recital (16) states that, "The setting up of a system operator or a transmission operator that is independent from supply and generation interests should enable a vertically integrated undertaking to maintain its ownership of network assets whilst ensuring effective separation of interests, provided that such independent system operator or such independent transmission operator performs all the functions of a system operator and detailed regulation and extensive regulatory control mechanisms are put in place"; and
- Recital (19) states that, "the full effectiveness of the independent system operator or independent transmission operator solutions should be ensured by way of specific additional rules. The rules on the independent transmission operator provide an appropriate regulatory framework to guarantee fair competition, sufficient investment, access for new market entrants and the integration of electricity markets. Effective unbundling through the independent transmission operator provisions should be based on a pillar of organisational measures and measures relating to the governance of transmission system operators and on a pillar of measures relating to investment, connecting new production capacities to the network and market integration through regional cooperation. The independence of the transmission operator should also, inter alia, be ensured through certain 'cooling-off' periods during which no management or other relevant activity giving access to the same information as could have been obtained in a managerial position is exercised in the vertically integrated undertaking. The independent transmission operator model of effective unbundling is in line with the requirements laid down by the European Council at its meeting on 8 and 9 March 2007".
- The requirements of the European Council referred to in recital (19) are contained in the 'Energy Policy for Europe' action plan agreed by the Council, which includes the following statement: "Taking note of the Commission's internal market report

and the final report following the sector inquiry on the gas and electricity markets, with the aim of increasing competition, ensuring effective regulation and encouraging investment to benefit consumers, the European Council: [...] taking account of the characteristics of the gas and electricity sectors and of national and regional markets, agrees on the need for: • effective separation of supply and production activities from network operations (unbundling), based on independently run and adequately regulated network operation systems which guarantee equal and open access to transport infrastructures and independence of decisions on investment in infrastructure; [...]"

- According to the Commission's interpretative note (22 January 2010, pages 4/5), "Although [the OU, ISO and ITO] models provide for different degrees of structural separation of network operation from production and supply activities, each of them is expected to be effective in removing any conflict of interests between producers, suppliers and transmission system operators. This means that they should remove the incentive for vertically integrated undertakings to discriminate against competitors as regards access to the network, as regards access to commercially relevant information and as regards investments in the network. The three models should create incentives for the necessary investments and guarantee the access of new market entrants under a transparent and efficient regulatory regime (recitals 11 and 12 Electricity Directive and recitals 8 and 9 Gas Directive). This requirement for effective separation should provide general guidance for the interpretation of the unbundling rules of the Directives".