



**Integrated Single Electricity Market (I-SEM)
Consultation on the Aggregator of Last Resort Framework**

SEM-14-106

A Submission by EirGrid plc.

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Contents

Executive Summary	3
Introduction.....	5
EirGrid Plc	5
Structure of the Main Response	5
Assessment of Options	6
Functions of the aggregator of last resort	6
Consideration of Commercial Aggregator Options.....	7
TSO as Commercial AOLR (Option 1 or 2).....	7
Consideration of the Passive Route to Market Option	8
TSO as passive AOLR (Option 3)	9
Potential Enhancements to the Passive Last Resort Route to Market	9
Conclusions.....	11
Appendix 1 – EU Legislation	12
Appendix 2 - Responses to the Consultation Questions	14

EXECUTIVE SUMMARY

EirGrid Group welcomes the publication of the consultation on the Aggregator of Last Resort (AOLR) Framework for the I-SEM and the opportunity to respond to the consultation.

We welcome the use of aggregators within the I-SEM and agree that they have an important role to play in providing a route to market for smaller generators. It is also important that a market exists for commercial entities to act in and the proposals for an AOLR should not impede on the emergence of commercial aggregators with the benefits that they can provide to participants.

The options put forward for consultation represent two options for an active commercial aggregator and one for passive provision of a route to market for wind generation through options defined within the market rules. We believe that the active commercial aggregator role exceeds that required for a last resort route to market.

Implementing the regulated service as an active commercial aggregator could result in higher costs for the member generators as it would require more senior staff and trading decision support applications than would be necessary for a last resort solution. Equally, if the service is successful, it may become more an aggregator of first resort and it could become a barrier to both entry and innovation by commercial aggregation participants.

EirGrid also believes that existing licences in both jurisdictions and European legislation would make it inappropriate for the TSOs to carry out either of the commercial aggregator options identified in the paper.

EirGrid believes the passive forecasting and data submission option provides the services that satisfy the need for a last resort solution while creating space for the development of competitive commercial risk management solutions from other participants. We believe that by including fixed rules around intraday trading, the passive forecasting and data submission option can be improved and provide all of the market interface services needed by smaller generators. In this context it may be appropriate to make this route to market available to small priority dispatch generators of all types.

In summary EirGrid proposes

- The passive AOLR offers the best fit to participant and market requirements
- The passive AOLR approach offers the possibility of extending AOLR functionality to smaller generator of all types and small demand participants. EirGrid would support this extension
- Implementation of the passive AOLR by EirGrid would be feasible under current legislation and licence. Should it be the desire of the SEM Committee, EirGrid would be willing to implement the passive AOLR for the I-SEM.
- It would be inappropriate for EirGrid to carry out directly, or contract for, a commercial AOLR role

INTRODUCTION

EIRGRID PLC

EirGrid Group welcomes the publication of the consultation on the Aggregator of Last Resort Framework and the opportunity to respond to these proposals.

Both EirGrid, and its subsidiary SONI, have been certified by the European Commission as independent TSOs, and are licenced as the transmission system and market operators, for Ireland and Northern Ireland respectively.

EirGrid and SONI, both as TSOs and MOs, have roles defined within the draft EU regulations that the I-SEM is required to comply with. We are committed to delivering high quality services to all customers, including generators, suppliers and consumers across the high voltage electricity system and via the efficient operation of the wholesale power market. EirGrid and SONI therefore have a keen interest in ensuring that the market design is workable, will facilitate security of supply and compliance with the duties mandated to us and will provide the optimum outcome for customers.

This response is submitted on behalf of all of the EirGrid licensees.

STRUCTURE OF THE MAIN RESPONSE

The first part of this document outlines EirGrid's view of the proposals, addressing the proposed functions of Aggregator of Last Resort (AOLR), the active commercial approaches and the passive, non-aggregated, data forecasting and submission approach. This includes comments with respect to any legal and licence issue that may arise should the TSO be assigned the role. We also suggest amendments to the passive approach.

The next section provides our conclusions, while appendices include answers to the consultation questions and a summary of the legal position, as currently understood.

ASSESSMENT OF OPTIONS

In this section, we set out the views of EirGrid with respect to the significant issues raised in the consultation document.

FUNCTIONS OF THE AGGREGATOR OF LAST RESSORT

EirGrid believes that the important question to be addressed is the problem that the last resort service is trying to solve. To consider this, we need to reflect on where the need came from and why there was such a support for this in the HLD consultation responses.

When the first four market design options for the I-SEM were proposed in February 2014, the option that was perceived as having the greatest need for an AOLR was Option 3. This is because Option 1 allowed portfolio bilaterals in the forwards timeframe, Options 2 and 4 provided forms of ex-post pools.

Option 3 as proposed was based on mandatory unit based participation in the day-ahead market. The consultation paper also discussed imbalance prices based on either a single or a dual price system though this was not explicitly in connection with Option 3. This was considered a difficult arrangement for wind generators as they would be forced to submit offers into the European day-ahead market, based on forecasts, and be exposed to possibly penal imbalance prices. The cost of participation by small market participants who currently do not have active trading desks was seen as one of the key barriers to entry to the day-ahead market.

The final HLD of the I-SEM included some significant variations from the proposed Option 3. Firstly, day-ahead participation is no longer mandatory. This means that submission of offers by small market participants is an elective choice and spilling into imbalance arrangements is an accepted, if undesirable, fall-back position. Secondly, imbalance pricing will be based on marginal pricing principles. This reduces the risk of penal prices at the ex-post imbalance settlement stage. Both of these changes significantly reduced the need for proactive aggregation of smaller variable generation as wind generators have a route to the balancing market with no penal prices and without having to invest in resources for day-ahead market participation.

It would appear; therefore, that the primary objective of the AOLR is to submit offers into the day-ahead and intraday markets on behalf of generators who don't intend investing in this bidding functionality themselves. EirGrid believes that the functions outlined for the AOLR under Options 1 and 2 go beyond what is required and that the functions should be limited to calculation and submitting data into "the DAM, IDM and BM on behalf of eligible generators" and "submission of nominations to the TSO". The additional functions specified under options 1 & 2 seek to enhance the services being offered and risk over-complicating the solution. While pooling of risk and assuming market responsibilities are beneficial, we would consider that these should be functions of a competitive commercial aggregator and not a regulated route to market of last resort.

CONSIDERATION OF COMMERCIAL AGGREGATOR OPTIONS

We consider that the options put forward in the consultation represent two regulated active commercial aggregator options and a passive non-aggregated option. We will consider each of these approaches in turn.

The active commercial aggregators (Options 1 &2) would require the registration of a trading entity in the I-SEM (the AOLR itself) which is responsible for bidding activity, settlement with the various settlement entities within the I-SEM and funds transfer. The AOLR would also operate its own “sub market” wherein its members would go through a registration process with the AOLR and would be subject to further settlement and funds transfer activities. As such, the AOLR would have to take on a considerable administrative role, and some associated credit risk, which we believe would be costly to both implement and operate. Indeed the systems and processes required for the implementation of those “last resort” solutions would appear to be of a similar scope to those required by the market operator for the I-SEM. It is also assumed that a commercial AOLR may be expected to take on activity on behalf of its members in the Capacity Remuneration Mechanism.

With the objective to “seek out optimal revenues” for its members, the commercial AOLR would need to invest in complex wind forecasting and trading decision analysis support tools. The commercial activity proposed under these models would involve the procurement of trading specialists operating on a 24/7 basis which would add significantly to the operational costs.

These options would appear to entail a high cost of implementation and operation.

It should also be considered that if a commercial AOLR is successful, this could restrict the emergence of commercial aggregators in the I-SEM with the risk that the AOLR becomes the aggregator of first resort.

TSO AS COMMERCIAL AOLR (OPTION 1 OR 2)

The consultation paper considers the assignment of the commercial AOLR role to the TSOs. EirGrid have considered this and would agree with the issues raised in the consultation with respect to potential for conflict of interest with our other licence obligations, as well as with European legislation.

Options 1 and 2 require the AOLR to be active in the market and seek the best prices on behalf of generators in the intraday market. They also require the AOLR to be a signatory to the market documentation, e.g. the Trading & Settlement Code in place of the generators. From a legal perspective, this would lead to a prima facie conflict of interest between EirGrid/SONI’s duties as TSOs and the activities proposed to be carried out by the AOLR.

Allocating a commercial aggregation role to the TSOs would also raise serious concerns

regarding compliance with REMIT¹ requirements (in particular, regarding the prohibition of insider trading under Article 3) and IME3² unbundling requirements. Further details are contained in Appendix A to this response.

There may be difficulties in mandating that the TSO, or any other entity, outsource this role. If outsourcing was to be utilised to resolve conflict of interest concerns this would imply a very low level of oversight and would not in our view be consistent with an entity being responsible for, or exercising responsibility over, a function. EirGrid notes that in the examples of counter trading and wind forecasting cited by the SEM Committee in the consultation paper³ there is no conflict or potential conflict of interest and EirGrid has not, and is not seeking, through contracting agents for the provision of services to diminish in any way its responsibility or exercise of responsibility over the relevant functions. EirGrid does not therefore concur with the view expressed in the consultation paper that the outsourcing of the AOLR function would largely mitigate any potential conflict of interest; however, as we outline below, while such conflict may exist in the case of an active commercial aggregator (Options 1 and 2) it is itself mitigated in the case of the passive option, Option 3.

CONSIDERATION OF THE PASSIVE ROUTE TO MARKET OPTION

We note that Option 3 does not involve the aggregation of the individual generators availing of this option under the market rules, nor does the operator of the scheme participate in settlement on behalf of the generation, and thus could be referred to as Last Resort Route to Market (LRRM) functionality, rather than an explicit role or entity.

EirGrid believes that the LRRM function would provide the simplest solution at least cost for market participants. Under this model, they would individually register in the I-SEM and be responsible for their own settlement. They would be paid directly from the market rather than having financial transactions with a third party. They would have to manage their own credit risk but by being a generator, this is less cumbersome than for a supplier participant. Offers can be submitted through the LRRM to the day-ahead market based on agreed parameters (for example, if wind generators don't want to be exposed to the European price floor, then offers could make use of a range similar to the price floor and cap used in the SEM).

This simpler formulaic, unit based implementation should be a cheaper solution than the active aggregated solutions proposed which could also provide potential customers of commercial aggregators with benchmark information in terms of risk management options, cost and

¹ Regulation (EU) No 1227/2011 of the European Parliament and of the Council on wholesale energy market integrity and transparency (REMIT) adopted on 8 December 2011.

² Under Directive 72/2009/EC in particular.

³ Paragraph 5.5.18 of the consultation paper.

performance. The performance of the passive rules based LRRM can be reviewed and improved through periodic review of the regulated rules, potentially on an annual basis.

EirGrid also believes that the passive LRRM option will not impede the emergence of commercial aggregators in the I-SEM as these will be able to offer better products, including risk and credit management as suggested under the more active AOLR options.

TSO AS PASSIVE AOLR (OPTION 3)

Under Option 3, a passive last resort route to market service provider is more a data processing entity on behalf of participants with no requirement to maximise revenue. Option 3 does not require the provider to take on market responsibilities; however, it would still be required to submit data for trades in the day-ahead market on behalf of generators. As the submission of data for trades would be “passive” and in accordance with a pre-determined set of regulated rules, this would mitigate any potential conflict with IME3 unbundling requirements and the licence prohibitions concerning TSO involvement in generation activities.

Further consideration should be given to the provisions of Article 3 of REMIT as the TSOs would have access to “inside information” (as defined in REMIT) and would also be disposing of wholesale energy products on behalf of generators, however, it is unlikely that there would be a conflict with these provisions as the TSOs would be undertaking this role in good faith without using any information which would be considered “inside information” for the purposes of REMIT.

POTENTIAL ENHANCEMENTS TO THE PASSIVE LAST RESORT ROUTE TO MARKET

The passive LRRM approach as set out in the consultation paper relies on a central market mechanism for pricing of volumes and therefore does not interact with the continuous intraday as set out in the I-SEM HLD. This represents a significant drawback for this proposal.

However, we believe continuous intraday participation is possible with this option. This can be managed by fixing bidding rules for all units availing of the service; for example, if the latest forecast suggests that output would be lower than that submitted into the day ahead market, offer data could be automatically submitted on the units behalf at intraday reference price - 10%; or if the wind forecast predicts increased output, the additional volume could be submitted into the market at intraday reference price +10%. If continuous reference prices are not available, then the day-ahead price for the given trading period can be used. This would deliver the mechanistic solution envisaged but without being dependent on intraday auctions being implemented or the need for the use of any discretion in the submission of data. The parameters needed for this participation (reference price, bid range) could be subject to change via consultation on the market regulated rules, including approval by the RAs. These can be set for a number of years at a time in the same manner as the current SEM parameters. This approach to intraday participation represents one possibility. It is envisaged that different

approaches, or refinements to this approach, will be considered in conjunction with the industry at the detailed design stage

Market registration could be streamlined for smaller generators to ease the burden and remove any barriers they may face. In this manner, the registration processes can be tailored to suit generators who are participating through the LRRM function and they should not be required to take part in certain stages that would be required of participants who will be proactively managing their own trading. This can take the form of reduced technical validations, less communications testing, etc.

As Option 3 is based on the implementation of a regulated rule set and each generator is separately and directly registered in I-SEM it could be possible to extend LRRM services to small priority dispatch generators of all types. Each type of generation, e.g. small biogas, may have its own rule set based perhaps on generator availability rather than wind forecasts.

CONCLUSIONS

EirGrid is of the view that Option 3 (which does not include aggregation of generation) represents the best fit to I-SEM's requirement for a last resort route to market.

The primary purpose of a last resort route to market should be to allow I-SEM's wholesale energy markets be accessed by smaller participants without an excessive administrative burden and at reasonable cost. While the LRRM function should be designed to allow a reasonable wholesale price to be obtained, the seeking of optimal market revenues and risk management strategies would more appropriately be a commercial aggregator's role. It is appropriate that there be some level of differentiation between the LRRM function and that of commercial aggregator(s). It is our view that Option 1 and 2 do not provide a good fit to these requirements.

Furthermore, it would not be appropriate for EirGrid to act, or employ an agent to act, as an AOLR as described under Options 1 and 2. As Options 1 and 2 require the AOLR to be active in the market, seek the best prices on behalf of generators and sign up to market documentation on behalf of the generators there are concerns that this would lead the conflict with REMIT and other legislation as well as the TSOs' Licences.

EirGrid believes that Option 3, enhanced with Intraday Trading capability, provides the best fit to I-SEM requirements, avoids the need for legislative change and would offer small scale generation of all types a cost effective last resort route to the wholesale energy markets without acting as a barrier to entry for commercial aggregators. However, the TSOs will need to give further consideration to design of the market rules to ensure that there are no perceptions of "inside information" feeding into the mechanism in contradiction to Article 3 of REMIT.

APPENDIX 1 – EU LEGISLATION

Article 3 of the Regulation on Wholesale Energy Market Integrity and Transparency (REMIT) provides for the prohibition of insider trading as follows:

1 Persons who possess inside information in relation to a wholesale energy product shall be prohibited from:

(a) using that information by acquiring or disposing or by trying to acquire or dispose of, for their own account or for the account of a third party, either directly or indirectly, wholesale energy products to which that information relates.

2 The prohibition set out in paragraph 1 applies to the following persons who possess information in relation to a wholesale energy product:

(c) persons with access to the information through the exercise of their employment, profession or duties.

As the TSO would have access to inside information, there is a conflict with Article 3 in relation to Options 1 and 2. In addition, the AOLR role would conflict with the IME3 unbundling requirements and the licence prohibitions concerning TSO involvement in generation activities.

Under Article 9.1(b) of the IME3 Directive⁴, the same person or persons are entitled neither:

(i) directly or indirectly to exercise control over an undertaking performing any of the functions of generation or supply, and directly or indirectly to exercise control or exercise any right over a transmission system operator or over a transmission system; nor

(ii) directly or indirectly to exercise control over a transmission system operator or over a transmission system, and directly or indirectly to exercise control or exercise any right over an undertaking performing any of the functions of generation or supply.

This is further set out in condition 20 of the EirGrid plc TSO Licence which states that:

1 The Licensee shall not and shall procure that any affiliate or related undertaking of the Licensee shall not, on behalf of the Licensee, engage in the generation, distribution or supply of electricity in the Island of Ireland.

Likewise, under Conditions 12 and 13 of the SONI Licence:

Condition 12: *2 For the purpose of facilitating its compliance with paragraph 1, the Licensee shall ensure that:*

(b) it does not hold or acquire shares in a holding company of the Licensee or in any electricity undertaking engaged in the generation or supply of electricity on the Island of Ireland;

Condition 13: *1 Except with the prior written consent of the Authority and in accordance with any*

⁴ Directive 72/2009/EC

conditions of that consent, the Licensee shall not purchase or otherwise acquire electricity for the purpose of sale or other disposition to third parties on the Island of Ireland, save to the extent it is necessary to do so in undertaking the Transmission System Operator Business.

It would appear from this that there are significant legal obstacles to designating the TSO as the AOLR for the I-SEM if adopting the proposed active commercial aggregator approaches.

APPENDIX 2 - RESPONSES TO THE CONSULTATION QUESTIONS

Question	EirGrid Response
<p>1. Do you agree with the potential functions of the AOLR as outlined? Are there any additional functions that the AOLR could potentially perform in I-SEM?</p>	<p>EirGrid believes that the functions outlined for the AOLR go beyond what is actually required. The core requirement for an aggregator (or IT system) is to facilitate day-ahead and intraday trading for generators who do not operate an active trading desk. As such, only the first of the proposed functions is required. The additional functions seek to enhance the services being offered and risk over-complicating the solution. While pooling of risk and assuming market responsibilities are beneficial, we would consider that these should be functions of a commercial aggregator and not a regulated route to market of last resort. As such, the functions should be limited to submitting data associated with "trading in the DAM, IDM and BM on behalf of eligible generators" and "submission of nominations to the TSO".</p>
<p>2. Which of the three models proposed in this paper do you think should be implemented? If none, are there alternative models to the ones proposed that should be considered?</p>	<p>While Options 1 and 2 have clear commercial benefits for participants in the aggregator, they potentially represent a greater conflict of interest for a regulated body assigned the roles. These options should be the functions and operations of commercial aggregators in the market rather than those of a last resort service. If the functions set out under Option 1 are successfully executed by the regulated aggregator, this could have the result of it becoming the aggregator of first resort and discourage the emergence of independent commercial aggregators as envisaged by the I-SEM HLD.</p> <p>Also, if Option 1 and 2 were assigned to the TSO as a role this would likely result in a costly implementation and would call into question IME3 certification. .</p> <p>Option 3, however, turns the core functions of forecasting and submission of trading data by the TSO into a mechanised, regulatory approved, rules driven process, without commercial optimisation by the party submitting the data. No aggregation takes place and the generators retain responsibility for market registration, credit cover etc. The main drawback of Option 3 is the lack of intraday trading. However, we</p>

	<p>would be of the opinion that this can be achieved with relatively low cost and little conflict by setting out explicit rules that must apply to intraday trades. For example, if the wind forecast suggests that output will be higher than that submitted into the day ahead market, it should offer at ID reference price -10%; or if looking to buy back due to a declining wind forecast , it should bid in at ID reference price +10%. If continuous reference prices are not available, then the day-ahead price for the given trading period can be used.</p> <p>This would deliver the mechanistic solution envisaged but without being dependent on intraday auctions being implemented or the need for commercial trading strategies that aim to maximise revenue.</p> <p>We believe with this modification Option 3 represents the best and most cost efficient approach for the implementation of a last resort route to market in the I-SEM.</p>
<p>3. Would you consider providing aggregation services in the new market? If so, would you consider being the AOLR service provider?</p>	<p>The TSOs would be well placed to fulfil the Last Resort Route to Market (LRRM) role for I-SEM as described under Option 3.</p> <p>Assigning the roles as described under Options 1 & 2 to the TSO would not be compatible with European legislation or indeed current licence conditions..</p>
<p>4. Should the RAs, or alternatively the TSOs, be responsible for establishing the AOLR framework and the subsequent procurement of the AOLR service provider? Outline reasons for your preferred option and if there are any further issues that merit consideration.</p>	<p>If Option 1 or 2 are deemed to be the preferred solution, then it would be more appropriate for the RAs to establish the framework and procure a service provider. EirGrid does not therefore concur with the view expressed in the consultation paper that the outsourcing of the AOLR function under Options 1 or 2 would largely mitigate any potential conflict of interest. Under Option 3, it should be possible to implement the last resort route to market under a set of I-SEM market rules/procedures. Such rules would be established and subsequently managed under the normal market design, governance and change control mechanisms.</p>
<p>5. If the TSOs are selected as the preferred agent for establishing the AOLR framework, should the TSOs carry out the function in house or outsource it to a third party through a competitive tendering process? Outline reasons for your preferred option and if there are</p>	<p>EirGrid considers Option 3 to be the most appropriate solution to the concerns that have triggered this workstream. As this is an option that an eligible generator can select under the market rules, rather than a separate aggregation service, it would be required to be undertaken by the TSOs in their role of developing, facilitating and complying with the I-SEM</p>

<p>any further issues that merit consideration.</p>	<p>trading and settlement code.</p> <p>EirGrid believes that should either of the commercial options be selected, any entity assigned the role of the AOLR should be allowed implement the role in the manner that entity considers to be most appropriate. Given the restrictions imposed by current licences and EU legislation, it would be inappropriate to mandate a obligation onto the TSOs to outsource this function given the implications on statutory compliance. In addition proper consideration of the marketplace for service providers of this function is essential, including the scope of any elements to be outsourced, along with the risk of forcing an outcome of a procurement process that may stifle competition and consequently not be in the public interest.</p>
<p>6. Do you believe the options for the AOLR proposed in this paper present a potential cross subsidisation of AOLR costs by others not involved with the AOLR?</p>	<p>This risk is more apparent for Options 1 and 2. The mechanical nature and transparency of Option 3 should help to mitigate this risk. Under Option 3, the allocation of costs between market participants would be defined in the overall market tariff framework.</p>
<p>7. Do you agree with the transparency measures proposed and if there is other information that should be disseminated to participants?</p>	<p>EirGrid has no opinion on this matter.</p>
<p>8. Do you agree that incentives are important for the AOLR? Are there other incentives that should be considered by the RAs?</p>	<p>As no aggregation takes place under Option 3, the performance of the route to market of last resort is largely determined by the efficacy of the related I-SEM rules and procedures. Such rules could be reviewed on a periodic basis to adapt to market conditions as they evolve over time. However, it will be important to ensure that incentives are limited to data processing accuracy and efficiency and that the TSO cannot be perceived to be benefiting from the prices obtained by generators who decide to take advantage of the regulated last resort service.</p>
<p>9. Do you agree with the issues raised surrounding cost allocation and the potential stranding of assets? Are there other issues that merit consideration?</p>	<p>This risk is greatest under Option 1 and 2. It is envisaged that this stage that Option 3 would largely be implemented as part of the larger systems required to support the wider I-SEM market, and would utilise the tools and systems that are also required for other purposes where cost-effective.</p>

<p>10. Do you agree that no upper threshold limit for wind participation in the AOLR should apply? If not, please propose a limit and provide reasons for this position.</p>	<p>It would seem appropriate the some threshold for participation should be in place. If small generation of any type is allowed to utilise the last resort service, this threshold would be necessary to preserve the unit participation principle in the I-SEM HLD. Aggregation of generation capacity under Option 1 or 2 (where the AOLR is the only market registered unit) would need to be limited in order to manage the system security risk of not knowing the location of a large block of generation. As each generator is separately registered under Option 3, this threshold may be higher as the geographical location of each generator is known.</p>
<p>11. Should smaller participants, other than wind, be considered eligible for participation to the AOLR? If you agree please outline the participants that merit consideration or if you don't agree please provide reasons.</p>	<p>If the main purpose of the last resort service is to allow small generation to avoid excessive administrative burden to access the wholesale market, then it would be reasonable to extend this facility to all priority dispatch generation types.</p>
<p>12. If participants other than wind should be included in the AOLR, should these be grouped for the purposes of bidding into the ex-ante markets and settlement given their respective risks in the new market design?</p>	<p>As with wind generation, EirGrid's view is that each generator should be registered directly with I-SEM. Risk pooling if desired could be achieved through a set of side arrangements outside of the AOLR function.</p> <p>It will be essential that the TSOs' ability to fulfil their statutory obligations related to system stability and security are maintained under any aggregation options in the I-SEM.</p>