



I-SEM Roles and Responsibilities Decision Paper

and

Next Steps on Synergies and Conflicts of Interest

SEM-15-077

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1 INTRODUCTION

1.1 BACKGROUND

The Integrated Single Electricity Market (I-SEM) and the European rules that underpin it will require the establishment of a number of new roles and responsibilities as well as changes in the responsibilities of a number of existing electricity licensees including the Market Operator, Transmission System Operators (TSOs), interconnector owners, generators and suppliers.

In anticipation of implementation of the I-SEM by Q4 of 2017¹, the SEM Committee (SEMC) published an 'I-SEM Roles & Responsibilities' consultation on 6 March 2015 (SEM-15-016)² regarding the allocation of key administrative roles and responsibilities amongst parties within the new market. These roles included:

- Balancing Market Operator;
- Settlement of Imbalances;
- Capacity Mechanism Delivery;
- Capacity Mechanism Settlement;
- Forward contracting.

Within the 'I-SEM Roles & Responsibilities' consultation, the SEM Committee provided a minded-to position on which entity operational roles for the I-SEM should be assigned to. In some cases, assignment was based on allocation of roles as defined by the European Network Codes or Guidelines – the Regulation on Capacity Allocation and Congestion Management (CACM) and the draft Electricity Balancing Network Code (EBNC); for other roles, the SEM Committee has given consideration to stakeholder opinion received³ in response to the 'I-SEM Roles and Responsibilities' Consultation, and to possible synergies which can be availed of in order to create an efficient market in terms of operational aspects and cost impact. It should be noted that some of the European Network Codes and Guidelines have not yet been finalised, and as such the assignment of roles in this decision may be subject to change should the intent of the draft codes change.

¹ [I-SEM Project Plan Quarterly Update August 2015 SEM-15-051 I-SEM Project Plan Quarterly Update August 2015.pdf](#)

² [SEM-15-016 I-SEM Roles and Responsibilities Consultation Paper SEM-15-016 I-SEM Roles and Responsibilities Consultation Paper.pdf](#)

³ Thirteen non-confidential responses were received and published here: http://www.allislandproject.org/en/TS_Decision_Documents.aspx?article=5d172226-e065-4bba-9ff9-80512012c885&mode=author

1.2 PURPOSE OF THIS DOCUMENT

The purpose of this decision document is to:

- Provide a synopsis of stakeholder responses to the I-SEM Roles & Responsibilities Consultation and which we have considered in our assignment of each of the I-SEM roles;
- Set out the SEM Committee's Decisions on assignment of operational roles for the I-SEM relating to the Energy Trading Arrangements and the Capacity Remuneration Mechanism;
- Indicate 'next steps' regarding implementation of governance and licensing arrangements for I-SEM, including plans for stakeholder engagement to provide for implementation of I-SEM by Q4 of 2017.

The I-SEM Roles and Responsibilities consultation stated that a separate exercise would be carried out regarding synergies, conflicts of interest and mitigation measures to deal with these. Instead, given the strength of responses to the consultation regarding this issue, the SEM Committee have decided to introduce a 'Governance Review Process' to explore any concerns further and allow more meaningful face-to-face engagement on the issue. As part of this, the SEM Committee will consider the synergies and conflicts of interest which exist not only in relation to the roles assigned in this decision, but also to the role of the East-West Interconnector within the EirGrid Group, while taking on board decisions stemming from the DS3 project.

1.3 ROLES CONSIDERED IN THIS DECISION

This paper provides the SEM Committee's Decisions on the assignment of roles for operation and settlement of the I-SEM energy market and capacity mechanism arrangements:

Energy Trading Arrangements (ETA) Roles

- Balancing Market Operator
- Settlement of Imbalances

Capacity Remuneration Mechanism (CRM) Roles

- Capacity Mechanism Delivery
- Capacity Mechanism Settlement

Other Roles

This decision paper sits alongside separate publications which outline the RAs' decisions on the Nominated Electricity Market Operator (NEMO) designation for I-SEM. The Capacity Allocation and Congestion Management (CACM) Regulation provides that the appointed NEMO will be responsible for Day Ahead and Intraday Market Operation. This was acknowledged by respondents to the I-SEM Roles and Responsibilities consultation, so the NEMO role is not discussed in this decision paper. CER and UR decisions on the NEMO designations (to EirGrid plc in Ireland and to SONI Ltd in Northern Ireland) were published separately on 2 October 2015⁴.

The recently published SEM Committee Decision (SEM-15-065) regarding the arrangements for an Aggregator of Last Resort (AOLR) provides for the mechanism and governance arrangements for the AOLR. Implementation of these decisions will be progressed through licence and code modifications as appropriate.

Roles regarding cross border capacity allocation for the forward timeframe, governance arrangements (relating to the single European Auction Platform and Harmonised Auction Rules) will come under the aegis of the Forward Capacity Allocation (FCA) Network Code and will be dealt with in the Forwards & Liquidity workstream decision which is scheduled to be published in Q4 2015. Changes to the licences of the Moyle and East West Interconnector may be required to implement the SEM Committee Decision on Financial Transmission Rights (FTRs) as well as to ensure consistency with the FCA Network Code/Regulation.

At this point, we do not envisage any specific roles or functions to be assigned for the Forwards and Liquidity and Market Power workstreams. Licence changes resulting from SEM Committee Decisions will be implemented in advance of I-SEM Go-Live.

1.4 GOVERNANCE REVIEW PROCESS – LICENCE AND CODE MODIFICATIONS

By way of 'next steps', the Departments (the Department of Enterprise, Trade and Investment in Northern Ireland and the Department of Communications, Energy and Natural Resources) are developing legislative changes that to accommodate the I-SEM, and the RAs will in conjunction develop changes or revisions to Codes and regulated licences.

Following publication of this paper and in order to implement the decisions on I-SEM roles and responsibilities, we intend to carry out a review of the SEM governance arrangements to ensure that changes are made to relevant licences and codes. This will include the development of adequate mitigation measures to address real or perceived conflicts of interest and realise synergies. We will organise stakeholder input and a workshop at the appropriate juncture.

⁴ http://www.allislandproject.org/en/TS_Decision_Documents.aspx?article=5d172226-e065-4bba-9ff9-80512012c885&mode=author

We intend to cover the following topics as part of the Governance Review process:

- **Energy Market Governance** –Market Operator licensing, regulation, provision for other NEMOs. Updating of SEMO licences for I-SEM roles;
- **Energy Trading Arrangements** – Aggregator Of Last Resort, licence changes/requirements from Energy Trading Arrangements Markets Paper including central dispatch provisions and new balancing arrangements as required ;
- **Capacity Remuneration Mechanism (CRM) Governance** – requirements for operating capacity auctions and administering capacity auction rules, provisions for capacity agreements or contracts as required and as set out in the Detailed Design Decisions of the CRM;
- **Mitigation of Conflicts of Interests** – Mitigation measures, licence related or otherwise, to ensure consumers are protected from any real or perceived conflicts of interests relating to I-SEM roles as set out in section 1.5;
- **EU Network Codes and Guidelines** –licence changes (if any are required) to align with EU Network Codes and European Commission Guidelines being developed under Regulation (EC) 714/2009 including Regulations on Capacity Allocation and Congestion Management, Forward Capacity Allocation and Electricity Balancing .

To support the Governance Review and ensure robust consideration of stakeholder views, the implementation of other key regulatory workstreams (I-SEM ETA and CRM implementation as well as DS3) will be taken into account when developing the required changes.

We expect significant changes either to the current Trading and Settlement Code, or in the form of a 'new' Trading and Settlement Code for I-SEM. The changes will primarily be in respect of the Energy Trading Arrangements, the Capacity Remuneration Mechanism and general governance. The SEM Committee recently consulted on proposals for the Trading and Settlement Code modification process for I-SEM⁵ (SEM-15-060). An Information Note (outlining how we will transition from SEM to I-SEM) will be published at the beginning of October with a more detailed I-SEM Rules implementation document due to be published in early December 2015.

⁵ http://www.allislandproject.org/en/wholesale_overview.aspx?article=6f7e50f6-068e-4f3b-9339-08180b7d33af

Changes to the obligations of the roles set out in this paper will be incorporated into the (modified or replaced) Trading and Settlement Code as well as other codes and rules as required, including NEMO and CRM Auction rules.

Other codes, notably the Grid Code, will also require amendment to provide for the I-SEM arrangements and changed roles, notably regarding the operation of the balancing market and changes to system dispatch as well as any testing requirements introduced as part of the new CRM or DS3 project.

New rules to underpin some of the roles assigned in this paper and elsewhere may also be required including capacity auction rules and trading and settlement rules for NEMOs.

The RAs will undertake a review of regulated licences, including those of generators, suppliers, TSOs and Interconnectors. Licensees will be notified of any proposed licence modifications as soon as practicably possible to ensure that approved licence modifications are in place to allow go-live of I-SEM by Q4 of 2017. It is likely that licence modifications will be consulted upon between Q2 of 2016 and Q3 of 2017 and come into force in advance of market trials and go-live.

1.5 SYNERGIES AND CONFLICTS OF INTEREST

Consultation

In the I-SEM Roles and Responsibilities Consultation Paper (SEM-15-016) we considered both the synergies of one entity carrying out several of the operational roles for I-SEM such that transaction costs to market participants are minimised, and balanced this with concerns around real or perceived conflicts of interests that could lead to increased costs to consumers and mitigation measures that might be required to minimise such conflicts.

We identified synergies as relating to:

- Cost savings associated with economies of scope
- Cost savings associated with economies of scale
- Reduction in transaction costs

We set out that the specific features of the I-SEM arrangements may mean that a single market operator covering all the administration and settlement functions (including those required to administer the day ahead, intraday, balancing, ancillary services and capacity markets) might be required if these synergies are to be realised, especially given the small size of the market and limited number of market players.

In terms of real or perceived conflicts of interests, we set out the following necessary steps to assess and identify steps to mitigate these:

1. the identification of the conflict and assessment of how the conflict balances against overall value for all-island consumers;
2. assessing the ability of the party to act on such a conflict;
3. assessing the incentive of the party to act on such a conflict; and
4. identifying mitigation measures to deal with the conflict.

In the I-SEM Roles and Responsibilities consultation, we specifically asked:

- *Are there synergies and economies of scope from having a single entity perform the I-SEM market operator roles, i.e. day ahead and intra-day, imbalance settlement and capacity settlement? If so, how would these lower costs to consumers?*
- *Do you think there are conflicts of interest arising from the same entity performing the market operator and TSO roles in the I-SEM? If so how would these increase costs to consumers and what mitigation measure could be put in place to deal with these?*

All respondents to the consultation commented on conflicts of interest:

EAI and most respondents argued that conflicts between EirGrid's role as TSO, MO and Interconnector owner need to be addressed. EAI note that in most other markets the market operator is completely separate from the TSO and pointed out that 'while this may be too onerous/costly a requirement for a small market such as I-SEM there should be sufficient business separation between the TSOs and NEMO (if SEMO is designated as a NEMO)'.

Energia commented that perception of a conflict of interest is sufficient to distort competition and deter investment and BGE argued that it is important that the TSOs and MO are functionally separate given their divergent objectives and even more so as the TSOs take on counterpart roles in the new arrangements.

Many respondents argued that ring-fencing of the East West Interconnector (EWIC) from other TSO roles should be undertaken as part of the RAs' consideration of I-SEM Roles and Responsibilities and many respondents were of the view that transparency and adequate legal/ functional separation is required with strict ring-fencing regarding financing structures.

EAI/SSE do not believe that the issue of EWIC ownership can be dealt with separately as part of the TSO certification process; Energia expressed disappointed that this aspect of this potential conflict of interest between EWIC and EirGrid plc has been left to be considered in the TSO certification process.

EirGrid acknowledged that there may be a perception that there is a potential for conflict of interest, and is interested to hear any industry view in this regard. EirGrid is willing to engage with the RAs to discuss how any such perception, should it exist, could be addressed in a manner that does not introduce additional unnecessary costs to consumers.

Regarding synergies, market participants also commented as follows:

EirGrid, IWEA and Energia were of the view that synergies could be obtained from combining the settlement of imbalances and the capacity mechanism.

PPB expressed a preference for the roles of Balancing Market Operator and Balancing Market Settlement to be performed by a single common counterparty and RES point out that it is important to recognise the size of the I-SEM compared to other markets, and to recognise where efficiencies can be made through a reduced number of entities required to carry out the different market functions or through existing entities providing services.

Power NI similarly note that in a relatively small market such as I-SEM, appointing a single body to multiple roles on a price controlled basis should bring implementation and operational efficiencies.

SEM Committee Response

Context – EirGrid Group and Licensed Entities

The SEM Committee acknowledges that respondents to the consultation expressed views on real or perceived conflicts of interest, synergies and appropriate mitigation measures to address these. We note that respondents focussed both on:

- potential conflicts of interest between the role of EirGrid in the I-SEM operational roles (balancing market operator; day ahead/intraday and Imbalance market operator and CRM delivery functions) and the role of EirGrid as owner of the East West Interconnector (EWIC) and
- potential conflicts of interest between the role of EirGrid system operation and market operator roles

Since the focus of stakeholder concerns related to the potential for conflicts of interest between the roles considered in this paper amongst licensed entities within the EirGrid Group, we set out below an illustration of the structure of entities within the EirGrid Group for context:

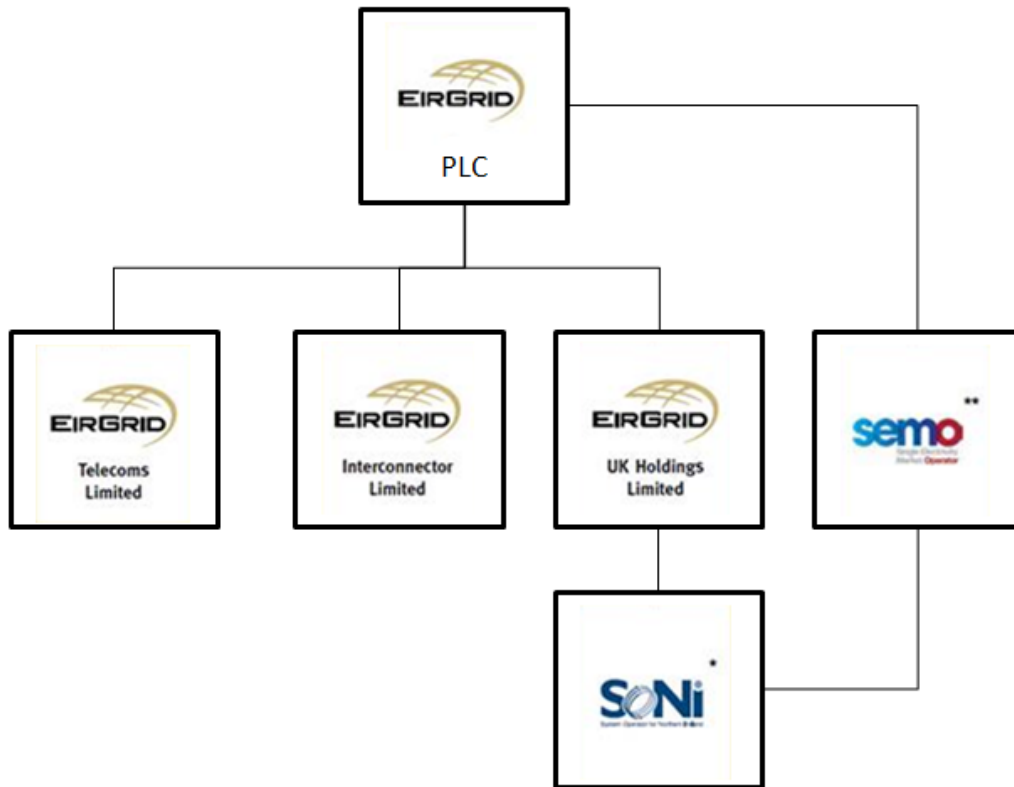


Figure 1: Structure of entities within the EirGrid Group⁶

In terms of the licenced entities which we considered when allocating I-SEM roles, the following are relevant:

- **EirGrid Plc** as the Transmission System Operator in Ireland
- **SONI Ltd.** as the Transmission System Operator in Northern Ireland
- **SEMO** as the contractual joint venture licensed to EirGrid plc and SONI Ltd
- **EirGrid Interconnector Limited** as a licensed Interconnector operator in Ireland and owner of the East West Interconnector. EWIC is due to undergo the process of certification as a TSO as required by Directive 2009/72/EC⁷.

Further work will be carried out to assess the levels of separation or ring-fencing currently in place amongst the EirGrid group structure and whether these are sufficient for I-SEM. This review will focus on the adequacy of current ring-fencing to address potential conflicts of interest. Discussions will take place with stakeholders as part of the Governance Review Process.

⁶ In addition, on 2 October 2015, EirGrid and SONI were designated as NEMOs in Ireland and Northern Ireland respectively.

⁷ Current and future transmission and interconnector licensees in Ireland and Northern Ireland are required to apply for certification under the ownership unbundling requirements of Directive 2009/72/EC which prohibits the same person or persons from directly or indirectly exercising control over a transmission system operator or over a Transmission system, and directly or indirectly exercising control or exercising any right over an undertaking performing any of the functions of production or supply.

Identification of Conflicts and Synergies

Regarding the various roles and functions of the above mentioned licensees and the new roles expected to be assigned for I-SEM, we consider that there are a number of synergies and potential conflicts of interests that may exist or arise. Table 1 sets out, at a high level, the magnitude of these synergies and the extent of the potential related conflict of interest:

Relationship	Synergies	Potential Conflicts	Note
TSO-MO/NEMO	Medium including expertise, hardware and systems, information procurement. Also, including internal economies of scope from common systems, benefits for external parties through reduced transaction costs.	Medium/Low: Risk that MO help TSO minimise Dispatch Balancing Costs rather than maximise efficiency and liquidity of DA and ID market May hinder effective representation of I-SEM in Europe; May prevent new NEMOs entering the market	-
Interconnector – TSO (BM, DS3 and CRM)	Low mainly consisting of shared corporate services.	High: Risk that design, operation, procurement and product development by TSO might favour Interconnector at expense of other service providers	Focus on regulation of TSO activities as it has ability to favour interconnector. Also consider adequacy of ring-fencing of EWIC.

Table 1: High Level Overview of Potential Synergies and Conflicts of Interest

Mitigation Measures

In the I-SEM Roles and Responsibilities Paper we set out a number of mitigation measures that could be applied to address conflicts of interest, including business separation or ‘ring-fencing’ requirements. These are set out in Table 2 below:

Level of ring-fence	Examples of business separation requirements
Information separation	restrictions on access to confidential information and computer systems
Employee and staff separation	separation of employee incentive schemes strict requirements affecting the transfer of employees from one business to another such as 3 month cooling off periods appointment and duties of a compliance monitor may ensure appropriate separation of staff as well as provide accountability for other separation measures
Physical separation	typically includes separation of property, facilities and premises
Financial separation and additional financial obligations	separate auditing and reporting of accounts separation of revenues and prohibition of cross-subsidy requirement not to hold or acquire shares or investments in other relevant business
Legal separation	requirement for directors to fulfil their roles as a director of a separate company whose sole business is the business in respect of which the legal board of which he is a member has been established

Table 2: Examples of Business Separation requirements

It is worth contextualising these measures in a wider set of mitigation ‘tools’ that the RAs may consider appropriate as part of a proportional response and evidence that potential conflicts of interest may increase costs to consumers. While, for example, legal separation is already in place for the East West Interconnector and separate reporting of accounts are in place for various roles (e.g. SEMO), additional measures will be required. This will be considered further during the Governance Review Process.

We consider that there are four main categories of mitigation measures, of which the above are a subset of structural and organisational remedies:

Mitigation Measure	Description
Ringfencing	The measures cover a spectrum of organisational or structural changes as set out in Table 2. They may be implemented in isolation or in combination with other measures. Some may be costly as they restrict the ability to exploit synergies.
Behavioural	These relate to Codes of Conduct for staff, incentives etc.
Control/Responsibility	These measures relate to regulatory oversight of market design including the energy market, the CRM and DS3 Auctions.
Transparency	Publication of information in a non -discriminatory manner, independent audit of functions under codes and licences

Table 3: High level Options for Mitigation of Conflicts of Interest

While we have not reached any conclusions on how to mitigate real or perceived conflicts of interest and suggestions for specific mitigation measures were not in general put forward by market participants, Table 4 below outlines more detail on possible mitigation measures with associated risks. Here we identify some of the possible conflict of interests that may arise in I-SEM and relevant options and considerations for mitigation including how such mitigation may impact on synergies across roles and functions. In Annex 1 we set out a table on how each issue will be progressed. Before considering the ‘possible mitigation measures’ in the second column, we will review the current level and adequacy of ring-fencing in place.

Examples*	Source of possible conflict	Possible mitigation measures*	Risks with Mitigation Measure
MO⁸ and TSO	1) TSO is not neutral to market outcomes (e.g. incentivised to minimise Dispatch Balancing Costs), which may distort MO incentives in operating the market.	Design: a) regulatory oversight of design of imbalance arrangements. b) process for robust stakeholder engagement by NEMO before and after European committee discussions Operation: a) transparency (auditing of MO in terms of market inputs and results) b) Code of conduct for MO staff, supported by training and monitoring c) Clarity of incentives for MO staff (e.g. financial rewards, and/or reporting lines)	There are risks of a loss of economies of scope, which reduce corporate overheads and hence cost of increased corporate overheads passed onto consumers. May hinder the relationship between TSO and MO in terms of synergies between market operation and dispatch, which is very important in near-term timescales in a high wind system like the I-SEM, and in delivering coordinated market change (e.g. synergies of TSO as CRM delivery body and MO as CRM settlement)
CRM delivery body (TSO) And IC Owner	1) Interconnector commercial values are not neutral to CRM outcomes, including de-rating. This could distort the efficiency of the CRM results, increasing costs to consumers in the long-term.	Design: a) regulatory oversight of design of CRM auctions b) regulatory sign-off of TSO procedures for operating the auction, including de-rating process Operation: a) transparency (auditing of TSO in terms of compliance with public procedures document) b) Code of conduct for TSO staff involved in CRM delivery, supported by training and monitoring c) Clarity of incentives for CRM delivery staff (e.g. financial rewards, and/or reporting lines)	Loss of economies of scope, which reduce corporate overheads (and hence costs to be passed onto consumers). Risk of distorting behaviour whereby the TSO excessively de-rates foreign capacity providers in CRM auction to demonstrate its independence from EWIC leading to consumers paying for more capacity than they would otherwise need to.

⁸ Including imbalance settlement

Examples*	Source of possible conflict	Possible mitigation measures*	Risks with Mitigation Measure
	<p>2) TSO can provide IC with information on product development and bidding patterns in CRM (this could distort the efficiency of the CRM results, increasing costs to consumers in the long-term)</p>	<p>Design: c) Interconnectors not bidding directly into the CRM Auction, i.e. GB and other non SEM generation participating in the CRM Auction. d) TSO to provide regular public updates on product development e) Obligations on TSO re. data confidentiality of information regarding bidding in CRM Auction f) Code of Conduct for staff involved in CRM Auction</p>	
Examples*	Source of possible conflict	Possible mitigation measures	Drawback of excessive mitigation
<p>Balancing market operator (TSO)</p> <p><u>And</u></p> <p>IC Owner</p>	<p>1) IC commercial value not neutral to its direction of flow in balancing timescales (e.g. could affect ability to access system service revenue, possibly displacing other more efficient providers and/or increasing total consumer payments directly)</p> <p>2) The related point that cross border flows can affect ability of other parties to provide system services</p>	<p>Design: a) regulatory oversight of design of balancing arrangements b) regulatory sign-off of TSO procedures for operating the balancing arrangements</p> <p>Operation: a) transparency (auditing of TSO in terms of compliance with public procedures document) b) Code of conduct for TSO staff involved in BM operation, supported by training and monitoring c) Clarity of incentives for TSO BM staff (e.g. financial rewards, and/or reporting lines)</p>	<p>Loss of economies of scope, which reduce corporate overheads (and hence costs to be passed onto consumers).</p>

Examples*	Source of possible conflict	Possible mitigation measures*	Risks with Mitigation Measure
	<p>3) TSO can provide IC with information on bidding patterns and product development in the balancing market (this could distort the efficiency of the BM results, increasing costs to consumers in the long-term)</p>	<p>Design: c) IC not bidding directly into the balancing market, rather that cross border balancing managed through TSO-TSO arrangements as per Balancing Network Code. d) TSO to provide regular public updates on product development</p>	
Examples*	Source of possible conflict	Possible mitigation measures	Drawback of excessive mitigation
<p>System services delivery body (TSO) And IC Owner</p>	<p>1) IC commercial value is not neutral to system services revenue (e.g. could possibly displace other more efficient providers and/or increasing total consumer payments directly)</p>	<p>Design: a) regulatory oversight of design of balancing arrangements b) regulatory sign-off of TSO procedures for operating the balancing arrangements Operation: a) transparency (auditing of TSO in terms of compliance with public procedures document) b) Code of conduct for TSO staff involved in BM operation, supported by training and monitoring c) Clarity of incentives for TSO BM staff (e.g. financial rewards, and/or reporting lines)</p>	
	<p>2) TSO can provide IC with information on bidding patterns and product development in the system services market (this could distort the efficiency</p>	<p>Design c) IC will act as price-taker in the system services auction d) TSO to provide regular public updates on product development c) RAs oversight and approval of DS3 Auction Rules</p>	

Examples*	Source of possible conflict	Possible mitigation measures*	Risks with Mitigation Measure
	of the system services results, increasing costs to consumers in the long-term)		
Examples*	Source of possible conflict	Possible mitigation measures	Drawback of excessive mitigation
Common settlement of energy markets and CRM (MO)	1) incentives for cross-subsidisation of NEMO (e.g. to deter new entry)	Operation: a) regulated revenue for SEMO, including benchmark allocation of shared costs against market rates	Strong business separation of NEMO from other settlement roles may risk losing benefits of 1) Reduced transaction costs (e.g. single registration; reduced credit and collateral combined invoicing) 2) economies of scope (e.g. shared corporate overheads, coordination of future market changes, shared metering data feeds)
	2) no scope for competition in wider MO role (deter new entry into NEMO role)		If enforce separation, then lose benefits of 1) Reduced transaction costs (e.g. single registration; reduced credit and collateral combined invoicing) 2) economies of scope (e.g. shared corporate overheads, coordination of future market changes, shared metering data feeds)

Table 4: Overview of Potential Conflicts of Interest, Possible Mitigation Measures, and risks with excessive application of Mitigation Measure

Next Steps

The SEM Committee is mindful of the need to strike the right balance between maximising synergies and mitigating measures for real or perceived conflicts of interest so that the long term interests of consumers are protected. In this sense it is important to ensure that market outcomes deliver value to end consumers such that the long term costs of potential conflicts of interest are balanced against and the costs of mitigation (direct and indirect costs – e.g. frustrating synergies, and distorting behaviour) and the powers available to the RAs to mitigate conflicts.

Based on the above discussion, we intend to develop our thinking further on potential conflicts of interest and synergies with the development of mitigation on a case by case basis. In addition, we will further review the level of current separation and any ring-fencing within the EirGrid Group. We intend to bring forward solutions through the establishment of a Governance Review Process, which will also allow effective wider stakeholder engagement and draw on experience of managing these issues to date as suggested by some respondents to the consultation.⁹

The intent of further stakeholder engagement will be to afford market participants a further opportunity to voice their views and concerns regarding the management of synergies and conflicts of interest in I-SEM. The Governance Review Process will be carried out in conjunction with the decisions and implementation of the I-SEM detailed design market rules via consultations and various stakeholder fora. I-SEM Detailed Design and implementation decisions (such as the ETA and CRM detailed market rules, CRM Detailed Design Decisions and Auction rules and DS3 decisions) will be developed in the context of the synergies and conflicts of interest discussed in this paper, and necessary licence and code changes will be developed as appropriate. In Annex 1 we set out a table on how each issue will be progressed.

In Q1 2016, following conclusion of the Governance Review Process, the RAs will publish an Information Paper outlining the mitigation measures we intend to put in place to ensure that real or perceived conflicts of interest are dealt with appropriately and synergies maximised, while ensuring value for consumers.

We intend to reflect the outcome of this process through changes to licences and contractual arrangements (such as the Trading and Settlement Code, Market Operator Agreement, assignment of TSO obligations under EU Network Codes, implementation of codes of conduct, audit provisions etc.) as appropriate and as set out in more detail in Annex 1.

⁹ e.g. Gas link and Gas Networks Ireland and other examples ring-fencing and behavioural or other mitigation measures currently in place for licences in Ireland and Northern Ireland

2 DECISIONS ON ASSIGNMENT OF I-SEM ROLES & RESPONSIBILITIES

2.1 ENERGY TRADING ARRANGEMENTS ROLES

Balancing Market Operator

Consultation

The Balancing Market Operator is the entity responsible for balancing the differences between supply and demand that occur on the electricity transmission system. Electricity balancing involves balancing energy (i.e. increasing or decreasing demand or generation to ensure they are balanced) and balancing reserves.

As set out in the recent SEM Committee I-SEM Markets Decision Paper¹⁰ the nature of system operation will change from SEM to I-SEM given the introduction of ex-ante contractual positions at the day ahead and intra-day timeframes and the resulting need to take both energy actions to balance supply and demand, and non-energy actions to ensure all constraints on the system are respected. The draft European Balancing Network Code (EBNC) also introduces requirements for the cross border operation of the balancing markets and obligations on operators of balancing market operators in each bidding zone of each EU Member state.

The SEM Committee's minded-to position in the I-SEM Roles & Responsibilities Consultation was to assign this role to the TSOs (i.e. EirGrid TSO/ SONI TSO), in line with the TSO licence conditions and the draft Electricity Balancing Network Code EBNC.

A number of responses were received from stakeholders on the balancing market operator role. IWEA, Bord na Móna, Energia and PPB agreed that the operation of the balancing market in the I-SEM is a core TSO function. Energia went on further to state that both the balancing Market Operator role and the Capacity Mechanism Delivery role should be TSO functions providing that potential conflicts arising from EirGrid's ownership of EWIC are eliminated.

SEM Committee Response

Given the central role of the TSOs in the operation of balancing markets in other jurisdictions and as part of their core functions, we do not see any reason to depart from the minded to position of the TSOs taking on responsibility for energy and non-energy balancing in the I-SEM.

SEM Committee Decision

In line with the TSO licence conditions to ensure a feasible dispatch of plant and to operate a safe and secure system the new responsibilities for the TSOs set out in the SEM Committee Decision on the ETA Markets and the draft EU Balancing Network Code, the SEM Committee determines that the Balancing Market Operator role for the I-SEM will be assigned to the TSOs.

We will review the TSOs' licences and Grid Code to establish the changes required with regard to the detailed design of the Balancing Market, notably around central dispatch and the detailed Balancing arrangements to be developed under the revised Trading and Settlement and cross border arrangements with National Grid in GB to ensure the efficient use of the interconnectors in real time as set out in the EBNC.

Regarding concerns relating to conflicts of interest between EirGrid role as operator of the balancing market and the EirGrid Interconnector Limited, we intend to address this as part of our consideration of synergies and conflicts of interest and appropriate mitigation measures through a Governance Review process and associated Code and Licence changes. The Governance Review Process endorsed by the SEM Committee is set out in section 1.4 of this paper, as is possible measures to mitigate conflicts of interest in section 1.5.

Imbalance Settlement Operator

Consultation

The imbalance settlement process settles discrepancies between the amount of electricity that a company has contracted to generate or provide through demand-side and the amount of electricity which the company actually generated or provided by demand side response. If a difference between forecast and actual exists, a party is regarded as being 'in imbalance' and these differences in quantity are settled at the imbalance price.

The ETA Markets Decision Papers¹¹ set out the design of the pricing and settlement of imbalances in the I-SEM and provide that Imbalance Settlement is the process which, for each Imbalance Settlement Period, settles:

- the differences between:
 - the quantity of electricity that a participant has contracted to produce or consume in the ex-ante markets (adjusted for any incremental offers and/or decremental bids accepted by the TSOs in the Balancing Market); and
 - the quantity of electricity that the participant actually produced or consumed; plus
- the incremental offers and decremental bids accepted by the TSOs in the Balancing Market.

The I-SEM HLD states that all market participants in I-SEM shall be balance-responsible and that imbalance settlement will be at the unit level for generation,

¹¹ http://www.allislandproject.org/en/wholesale_overview.aspx?article=95576707-dd90-479a-b631-630178cca133&mode=author

with possible exemptions for certain renewables, and for dispatchable demand. The SEM Committee have determined in the ETA Market Decision Paper that a system of ‘flagging and tagging’ will be implemented to determine the marginal imbalance price in the I-SEM.

The entity responsible for imbalance settlement will therefore be required to:

- Determine the imbalance price or prices for each settlement period as per the ETA Markets Decision Paper and;
- Administer a set of market rules for the settlement of imbalances, to be included in the revised Trading and Settlement Code;
- Provide collateral arrangements to limit exposure from non-payment;
- Provide a system of registration, funds transfer, invoicing, resettlement and rules for the management of currency risk.

We proposed in the I-SEM Roles & Responsibilities Consultation that the role of Imbalance Settlement Operator should be assigned to either the TSOs or the current Market Operator (the Single Electricity Market Operator).

We received a mixed response to the consultation regarding the minded-to position for the Imbalance Settlement role. PPB were in agreement with the SEMC in that the role of Balancing Market settlement could be performed by the TSO or a market operator. Bord na Móna and IWEA instead remarked that settlement functions can be administered by the Market Operator. EirGrid commented that settlement of balances and imbalances are currently undertaken by EirGrid and SONI under their Market Operator licences. EirGrid therefore noted the default position, as outlined in the Network Codes that this function will be carried out by the TSOs.

Many respondents pointed to the significant synergies of having a single market operator performing all market settlement functions including imbalance, capacity, day ahead and intra-day. Some respondents questioned why the role of imbalance settlement was being considered in isolation from other market timeframes such as day ahead and intra-day and the designation of NEMOs.

SEM Committee Response

The SEM Committee welcomes respondents’ views on the role of imbalance settlement. While we appreciate the need to realise synergies in the I-SEM the designation of NEMO roles come under a new process outlined in the CACM Regulation where applications for day ahead and intra-day market operators are assessed against the criteria in the CACM Regulation and therefore must be considered separately to other administrative roles in the market.

From a European and cross border trade perspective, the current draft of the EBNC places the obligation for imbalance settlement on the TSOs. However, while dispatch and balancing of the electricity system in real time is a core TSO function, imbalance settlement is not. The ENBC provides that the function of imbalance settlement may be assigned by the TSO to a party other than a TSO if provided for in current legislation or upon request of the TSOs. The assumption in European cross border rules is therefore that imbalance settlement is carried out by the TSOs unless provided for elsewhere in legislation or upon request by the TSOs to delegate this function.

In order to maximize synergies across different market timeframes whilst mitigating any potential conflicts of interest between the TSOs core roles and market administration we consider that SEMO should be responsible for imbalance settlement in the I-SEM.

SEM Committee Decision

The SEM Committee Decision is that, to take advantage of synergies and mitigate conflicts of interest, imbalance settlement will be carried out by the Single Electricity Market Operator (SEMO).

Electricity Market Operator and that therefore formal designation from the TSOs for this role is not necessary. Under Condition 3 of its licences In Ireland and Northern Ireland, SEMO is responsible for ‘entering into and at all times administering and maintain in force, the Single Electricity Market Trading and Settlement Code’.

We intend to develop the detailed market rules for I-SEM for incorporation into a revised Trading and Settlement Code; a paper outlining the process which we will follow is due to published at the start of October. We also expect to make changes to the SEMO licences to reflect these changes through the Governance Review process.

Furthermore, as EirGrid and SONI have been designated as a Nominated Electricity Market Operator (NEMO) for the Day ahead and Intra-day market there are clear synergies from having SEMO perform the imbalance settlement function, whilst recognising that further NEMOs may be designated or operate in the I-SEM in the future.

2.2 CAPACITY REMUNERATION MECHANISM ROLES

Delivery of the Capacity Remuneration Mechanism

Consultation

While the SEM Committee will oversee the design of the I-SEM capacity mechanism and its implementation through the approval of a set of capacity market and settlement rules, we will require a ‘Delivery Body’ to lead the implementation.

The Capacity Market Delivery Role is expected to include:

- Proposing the capacity requirement (that is the amount to be auctioned based on a pre-defined security standard) including the de-rating of capacity providers as required which the SEM Committee will subsequently approve;
- Implementing the SEM Committee's policies via preparation, pre-qualification and operation of auctions as well as planning the auctions and publishing results;
- Provision to the entity responsible for settlement of data and auction results necessary to settle capacity contracts and levy charges on market participants;
- Test providers to ensure those providers are able to demonstrate their capacity and validate eligibility of parties for secondary trading;
- Maintain a system or central register of capacity agreements or take on contractual counterparty to capacity contracts as appropriate.¹²
- Maintain a set of capacity market rules to be approved by the SEM Committee.

As is standard in other jurisdictions where capacity mechanisms are implemented (Great Britain, Italy, New England ISO, and PJM) and in line with their statutory duties regarding security of supply, we proposed in the Roles and Responsibilities Consultation that the TSOs would be the Delivery Body for the new capacity mechanism in Ireland and Northern Ireland.

Most respondents concurred with the SEM Committee's minded-to position. AES agreed that the TSO is uniquely placed at the centre of the system to undertake analysis and inform the RAs on capacity adequacy, system services requirements and a detailed understanding of the technical capabilities of all technologies on the island, particularly in the balancing system.

Bord na Móna was similarly of the view that it is appropriate that the TSOs should carry out the role of the delivery body for the capacity mechanism.

Bord Gáis was of the view that the Capacity auction could be undertaken by the Market Operator, arguing that the synergies would imply that the MO should also run Capacity Mechanism auctions. The majority of the new requirements of the Capacity Mechanism are commercial or administrative in nature (e.g. pre-

¹² The Counterparty arrangements for the CRM will be determined in CRM Decision 1 due for publication in early November.

qualification, auctions, contractual counterparty, collateral requirements) and the TSOs should not stray into the commercial workings of the Capacity Mechanism.

EirGrid agreed with the SEM Committee minded-to position that some of the functions of the CRM delivery body are core TSO roles that are currently carried out by the TSOs and that it is standard on other markets where capacity mechanisms are implemented that the TSOs be the delivery body.

Energia was of the view that the Capacity Mechanism Delivery role should be TSO functions providing that potential conflicts arising from EirGrid's ownership of the East West Interconnector are eliminated. Energia also noted that the design of the capacity delivery body should be considered separately to the Roles & Responsibilities consultation process.

SSE noted that the design of auction rules (commercial) must be strictly separated from the delivery body function (operational) and stated that the RAs should not be in a position where they were dependent on TSO information for the design of auction rules.

SEM Committee Response

We acknowledge stakeholders views on the capacity mechanism delivery role and general agreement that this should be assigned to the TSOs.

Regarding Bord Gáis' point relating to the Market Operator being responsible for the delivery of the Capacity Mechanism, we appreciate that there may be synergies between the market operation functions for I-SEM and the CRM auction, however we do not believe these to be significant. Furthermore, given that the procurement of ancillary services is a TSO function and the TSOs are responsible for the implementation of the DS3 auctions we consider the synergies between the CRM and DS3 auctions to be of greater significance, particularly in terms of the need to ensure coordination between auction of the CRM and DS3 products to ensure that consumers are not subject to double payments and that new investment is coordinated.

With regard to conflicts of interest relating to the CRM delivery role we acknowledge market participants responses and note the importance of restrictions on access to information in auctions as well as transparency (publishing) and independent auditing of the TSOs operation of the auction. As stated above we plan to address conflicts of interest through the implementation of proportionate mitigation measures to be developed through a Governance Review Process set out in section 1.4 together with consideration of mitigation measures as set out in section 1.5.

SEM Committee Decision

The SEM Committee Decision is that the TSOs will be responsible for delivery of the Capacity Remuneration Mechanism including administration and prequalification for the capacity auctions and administration of a set of capacity market rules subject to approval and oversight by the RAs.

While the precise detail of the regulatory framework to include licence changes required for the I-SEM CRM have yet to be determined, it is our expectation that we will introduce changes to the TSO licences to require them to perform the capacity mechanism delivery role and administer a set of capacity market rules approved by the SEM Committee.

Settlement of Capacity Payments and Charges

Consultation

As well as delivery and administration of the capacity market (i.e. the auction), a single entity will be responsible for the collection of charges and the distribution of payments to capacity providers (including Reliability Option difference payments). This will include the collection of all data necessary for that determination from the Capacity Delivery Body and metered settlement and pricing data, and the management of disputes relating to that data. Given that the new capacity mechanism is a centralised 'single buyer' model it is important that capacity charges are levied on all metered load. Further details of how we propose the settlement of capacity charges and payments to be designed are set out in the CRM Detailed Design Consultation Paper¹³ and the detailed settlement rules will be incorporated in the revised Trading and Settlement Code.

¹³ http://www.allislandproject.org/en/wholesale_overview.aspx?article=4f400a98-6fc8-476e-892d-de81be0ca53a&mode=author

The SEM Committee provided an initial minded-to position that the same entity responsible for the 'Settlement of Imbalances' roles would carry out this function.

A range of views were received from stakeholders regarding assignment of this role.

Energia agreed with the original SEM Committee position that the Capacity Settlement role should be carried out by the entity responsible for settlement of imbalances. Similarly, IWEA supported the proposal that capacity settlement be carried out by the entity responsible for imbalance settlement.

In contrast, Bord na Móna was of the view that settlement functions can be administered by the Market Operator and AES flagged concerns that the TSO is currently not equipped to host a CRM auction or administer the settlement of a CRM RO process and could incur considerable costs to establish these structures and processes – notably the function of a central counter party. BGE were also of the view that the Market Operator would be best placed to carry out settlement requirements and agreed with our minded-to position that cost and administration synergies apply to having capacity settlement carried out by the same entity responsible for imbalance settlement.

SEM Committee Response

Having considered the mixed responses received regarding the Capacity Settlement role, we continue to be of the view that settlement of the capacity market for I-SEM is best carried out by the same entity that is responsible for imbalance settlement given the synergies between the two functions in terms of payments to generators and levying of charges on suppliers for capacity and energy imbalances.

Given our decision above that SEMO should be responsible for imbalance settlement in the I-SEM and the related decisions on the NEMO designation (published on 2 October 2015¹⁴) we consider that there are significant synergies that can be realised from the Market Operator for other timeframes carrying out the settlement of capacity payments and charges. Depending on the reference market that is chosen for the reliability options in I-SEM and how supplier charges are profiled there will be significant interaction between the distribution of energy payments/collection of charges and the collection of capacity payments and charges.

SEM Committee Decision

The SEM Committee Decision is that, in order to maximize synergies and lower transaction costs in I-SEM, the Single Electricity Market Operator (SEMO) will be responsible for the function of capacity mechanism settlement; this is consistent with the minded-to position provided in the consultation that the same entity would be responsible for settlement of imbalances.

2.3 Nominated Electricity Market Operator for Day Ahead and Intra Day Market Coupling

This decision paper sits alongside separate publications which outline the RAs' decisions on Nominated Electricity Market Operator (NEMO) designation for I-SEM.

It is an EU requirement (via the CACM guidelines) that the appointed NEMO will be responsible for Day-Ahead and Intraday Market Operation.

CER and UR have designated EirGrid plc and SONI Ltd as NEMOs in Ireland and Northern Ireland respectively for an initial period of 4 years and subject to conditions set out in those decisions.

Following publication of this decision paper, we intend to review the current licence framework for the TSOs and MO roles and as part of this will consider how the NEMO functions are incorporated into those licences.

3 CONCLUSIONS AND GOVERNANCE REVIEW PROCESS

Conclusions

This document provides the SEMC's Decisions on the assignment of roles for:

- Energy Balancing Market Operator
- Settlement of Energy Imbalances
- Capacity Mechanism Delivery
- Capacity Mechanism Settlement

The SEM Committee has considered stakeholder views, particularly those regarding synergies and conflicts of interests, and has sought to minimise costs to consumers across the I-SEM administration and operational roles. We intend to address conflicts of interests, including implementation of proportionate mitigation measures, in a subsequent work deliverable through a Governance Review process.

The SEM Committee's Decisions are set out in Table 5 below:

Table 5: SEM Committee Decision on Assignment of I-SEM roles¹⁵

Role	<i>SEMC minded-to position in consultation</i>	SEMC decision
Balancing Market Operator	<i>TSOs</i>	TSOs
Settlement of Imbalances	<i>either the TSOs <u>or</u> current MO</i>	SEMO
Capacity Mechanism Delivery	<i>TSOs</i>	TSOs
Capacity Mechanism Settlement	<i>either the TSOs <u>or</u> current MO</i>	SEMO

Governance Review Process

Following publication of this decision our next steps in the process are to implement the changes required to effect the decisions in this paper and the simultaneous initial NEMO designations. This will include mitigation measures to address conflicts of interest, particularly with regard to the new roles being assigned to the TSOs and

¹⁵ It should be noted that where the SEMC decision refers to assignment to "TSOs", this should be taken as meaning assignment to EirGrid TSO and SONI TSO.

Market Operator for I-SEM implementation and operation, notably the CRM Auction and NEMO roles.

This implementation will be progressed through a **Governance Review Process** which will commence in October 2015 to review the necessary licence and code modifications for the TSOs and MOs resulting from this decision and other I-SEM and EU Network Codes changes. Further information regarding the Governance Review Process will be published on the AIP website in due course.

Any proposals for licence or code amendments resulting from the governance review will be published in a timely manner as soon as workstream decisions are made throughout 2016 and 2017. Annex 2 sets out our plans and timetable for implementation of the issues and Decisions in this Paper as well as other changes to roles and responsibilities for I-SEM and implementation of EU Network Codes.

The I-SEM Team will continue to engage with the Department of Communications, Energy and Natural Resources (DCENR) and the Department for Enterprise, Trade and Investment (DETI) in Ireland and Northern Ireland respectively regarding legislative changes.

Annex 1: Possible Mitigation Measures to deal with Potential Conflicts of Interest and Implementation Process¹⁶

Possible mitigation measures	Where taken forward
TSO – Market Operator (including imbalance settlement)	Governance Review Process, Licence and Code Changes
Design: a) regulatory oversight of design of imbalance arrangements	
b) process for robust stakeholder engagement by NEMO before and after European committee discussions	
Operation: a) transparency (auditing of MO in terms of market inputs and results)	
b) Code of conduct for MO staff, supported by training and monitoring	
c) Clarity of incentives for MO staff (e.g. financial rewards, and/or reporting lines)	
d) Separation of some information: MO can only provide TSO staff with information on same basis as would be released to any other party	
CRM delivery (TSO) – IC Owner	Governance Review Process, CRM Detailed Design Decision 1, Licence and Code Changes
Design: a) regulatory oversight of design of CRM auctions	
b) regulatory sign-off of TSO procedures for operating the auction, including de-rating process	
Operation: a) transparency (auditing of TSO in terms of compliance with public procedures document)	
b) Code of conduct for TSO staff involved in CRM delivery, supported by training and monitoring	
c) Clarity of incentives for CRM delivery staff (e.g. financial rewards, and/or reporting lines)	
Design: c) IC not bidding directly into the CRM auction	
d) TSO to provide regular public updates on product development	
TSO (BM operator) – IC owner	Governance Review Process, Implementation of ETA rules in TSC
Design: a) regulatory oversight of design of balancing arrangements	
b) regulatory sign-off of TSO procedures for operating the balancing arrangements	
Operation:	
a) transparency (auditing of TSO in terms of compliance with public procedures document)	
b) Code of conduct for TSO staff involved in	

¹⁶ Note that the RAs will also review what level (and adequacy of) ring-fencing is currently in place

Possible mitigation measures	Where taken forward
BM operation, supported by training and monitoring	
c) Clarity of incentives for TSO BM staff (e.g. financial rewards, and/or reporting lines)	
Design: c) IC not bidding directly into the balancing market	
d) TSO to provide regular public updates on product development	
TSO (DS3 Delivery) – IC Owner	Governance Review Process, Licence and Code Changes, Approval of DS3 Auction Rules
Design: a) regulatory oversight of design of balancing arrangements	
b) regulatory sign-off of TSO procedures for operating the balancing arrangements	
Operation: a) transparency (auditing of TSO in terms of compliance with public procedures document)	
b) Code of conduct for TSO staff involved in BM operation, supported by training and monitoring	
c) Clarity of incentives for TSO BM staff (e.g. financial rewards, and/or reporting lines)	
Design c) IC will act as price-taker in the system services auction	
d) TSO to provide regular public updates on product development	
MO – NEMO	
Operation: a) regulated revenue for NEMO, including benchmark allocation of shared costs against market rates	Governance Review Process, Licence and Code Changes

Annex 2: ROLES and REPONSIBILITIES ISSUES FOR THE DETAILED RULES AND IMPLEMENTATION PHASE

Issue	Responsible	Timeframe for Decision/Implementation
1 Develop of revised governance rules for I-SEM to take into account changes to roles and responsibilities	Mods Committee, RAs	October 2015 to December 2016
2 Development of measures to mitigate conflicts of interest and realise synergies for TSOs and MO roles	RAs	October 2015 to February 2016
3 Implementation of TSO Licence changes for I-SEM Roles	RAs, TSOs	Q2 2016 Consultation on licence changes
4 Implementation of MO licence for I-SEM Roles	RAs, MO	Q2 2016 Consultation on licence changes
5 Implementation of TSO and licence changes to reflect new obligations under EU Network Codes	RAs, TSOs	Q2 2016 Consultation on licence changes
6 Implementation of measure to mitigate conflicts of interest and realise synergies for TSOs and MO roles through licence and code amendments	RAs	Q2 2016 Consultation on licence changes and updating of other governance arrangements (TSC & codes) as appropriate.