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Consultation on proposed approach to cost recovery in relation to Capacity Allocation and Congestion Management mechanisms for electricity interconnectors

Dear Andrew

Thank you for the opportunity to provide views in relation to the proposals set out in the above-named document. This response is on behalf of Moyle Interconnector Ltd, owner of the 500MW HVDC interconnector between Northern Ireland and Scotland which provides a link between the SEM¹ and GB electricity markets.

Capacity allocation on the Moyle Interconnector is currently via explicit capacity auctions and implicit intraday capacity auctions that are part of the SEM arrangements. Capacity on Moyle is due to be allocated via the single day ahead market coupling from May 2018 as part of the I-SEM² arrangements and an interim intraday capacity allocation is to be implemented from the same point, with XBID expected to be implemented on the SEM-GB border by 2020 at the earliest.

Moyle Interconnector Ltd is a mutualised business, meaning that it has no shareholders and is 100% debt financed, underwritten by electricity consumers in Northern Ireland³. This means that any revenue shortfalls are funded by Northern Irish consumers and likewise, they may benefit from surpluses but consumers across SEM and GB enjoy the benefits of this interconnection.

Our primary concern with Ofgem's proposal is that it may result in Northern Irish consumers bearing GB consumers' 'share' of what are termed CACM development costs despite societal benefits of market coupling being enjoyed by stakeholders in both jurisdictions, which may not be consistent with underlying regulations. If Ofgem deems that efficiently incurred development costs can be recovered, this should be via GB network tariffs rather than from interconnector TSOs.

¹ SEM is the single electricity market in Northern Ireland and Ireland.

² I-SEM is the name given to the project to redesign the electricity market of Ireland and Northern Ireland to implement the European Target Model in accordance with EU Directive 2009/72/EC, Regulation (EC) No 714/2009, Regulation (EC) No 713/2009, and Commission Regulation (EU) 2015/1222. The I-SEM energy trading arrangements are due to go live in May 2018.

³ The mechanism for this is via the Moyle Participation in Transmission Licence issued by the Northern Ireland Authority for Utility Regulation



Operating costs under CACM

We agree with Ofgem that the operational costs are to be borne by NEMOs as they relate NEMO tasks under CACM article 7 and should be borne by NEMOs under CACM article 76.1(c). We also support the proposal that equivalent arrangements should apply to NEMOs 'passporting' into GB.

Development costs for pilot projects

We note Ofgem's proposal that efficiently incurred development costs in relation to the CACM Pilot Projects by the Power Exchanges' (designated as NEMOs under CACM) will be allowable against TNUOS (through reimbursement by interconnector TSOs). We support the idea that these development costs are recoverable through TNUOS as the implementation of these projects benefits the GB consumer by contributing to meeting the objectives of CACM and the internal energy market including "maintaining security of energy supply, increasing competitiveness and ensuring that all consumers can purchase energy at affordable prices".

While the proposal is not clear on this point, the statement 'through reimbursement by interconnector TSOs' suggests that the risk of NEMO costs being judged as inefficient would sit with the interconnector TSOs involved in the pilot projects – in our view NEMOs are best-placed to control the efficiency of their costs and should bear this risk, as other regulated entities do. However, we are not party to the pilot projects so are not aware of the governance and regulatory arrangements around this issue.

Development costs under CACM (enduring arrangements)

We believe that Ofgem's enduring proposal on recovery of CACM development costs requires further consideration and clarity.

Congestion revenue as cost recovery

It is our view that congestion revenues cannot be considered a cost recovery mechanism. It appears that this proposal does not align with article 16.6 of regulation (EC) No 714/2009, which is the predecessor of CACM and remains in effect. While CACM article 76.2 makes provision for TSOs to voluntarily make a contribution to the NEMO costs, this clause specifically refers to recovery through network tariffs or other appropriate mechanisms. Congestion revenues do not appear to be an appropriate mechanism and, if Ofgem wish to allow NEMOs to recover their costs via network tariffs, then a recovery route could be implemented via the national TSO in GB.

If interconnectors and the CACM arrangements are functioning well in terms of bringing bidding zone prices closer together then congestion revenues will be reduced since they are based on the price difference between bidding zones. The logic for these revenues being considered as a cost recovery mechanism is therefore unclear as there is no opportunity to increase them to recover costs. We note the rationale "*providing the capability for market coupling is a fundamental part of the product Interconnector TSOs offer to the market, we propose that the enduring arrangement for this capability should be paid for through the Interconnector TSO' congestion revenues*". The product that interconnector

TSOs offer to the market is a regulatory obligation, as is development of market coupling. It does not follow that market coupling is developed to support the interconnector product offering – the latter complements the former, rather than driving it. Development of market coupling is a legal requirement and CACM article 75.1 indicates that TSO costs related to such CACM obligations may be recovered⁴

NEMO development costs borne by interconnectors

CACM article 7.2(a) states that NEMOs are responsible for “developing and maintaining the algorithms, systems and procedures for single day-ahead and intraday coupling”. As with operating costs, CACM article 76.1 states that NEMOs shall bear the costs of “establishing, updating or further developing” the algorithms for day-ahead and intra-day coupling. It is unclear that interconnector TSOs are best-placed to ensure that NEMO development costs are reasonable, efficient and proportionate when they are incurred and controlled by NEMOs, who own the IT systems and supporting infrastructure. As stated above, in our view NEMOs are best-placed to control the efficiency of their own costs and should bear the risk that regulators do not consider them to be reasonable, efficient and proportionate for cost recovery purposes, where applicable.

Equity of the proposal

We do not believe that allocating GB’s share of the development costs, particularly GB NEMO costs, to interconnectors is an equitable proposal for GB’s neighbours. In the case of the interconnectors to SEM (Moyle and EWIC), these assets and the revenue they generate are effectively owned by electricity consumers in SEM. Use of these revenues to fund GB’s share of costs associated with developing XBID and day ahead market coupling means GB consumers are being subsidised by their neighbours despite sharing the benefits of these projects. To a lesser extent this issue is also relevant for the other GB interconnectors whereby RTE, for example, could end up paying for both French and GB development costs.

Timing issues

The proposed decision on CACM pilot project development costs indicates that these costs will be socialised (recovered via TNUOS). The pilot project will have considered only the specificities of those parties involved in it. This means that these parties will have substantially all of their specific development costs socialised while interconnector TSOs joining the day ahead market coupling or XBID after August 2015 and February 2017 respectively would pay for these through their congestion revenues. It is unclear how this differing treatment is warranted.

The implementation timelines for day ahead market coupling and XBID on the SEM-GB border are different to those parties involved in the pilot projects. It is unclear when and how the SEM-GB interconnector TSOs would become responsible for CACM development costs under the proposal. We note that interconnector TSOs may be expected to determine appropriate arrangements but are conscious that this may not be straightforward due to competing views.

⁴ “Costs assessed as reasonable, efficient and proportionate shall be recovered in a timely manner through network tariffs or other appropriate mechanisms as determined by the competent regulatory authorities.”

As a final point, we would query why 'MCO designation' is only considered the relevant start point for the enduring arrangements for XBID and not the day ahead arrangements.

We would be happy to discuss this topic and if you require any further information about any aspect of this response, please do not hesitate to contact me.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Paul McGuckin', with a stylized flourish at the end.

Paul McGuckin