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| **MODIFICATION PROPOSAL FORM** |
| **Proposer***(Company)* | **Date of receipt***(assigned by Secretariat)* | **Type of Proposal***(delete as appropriate)* | **Modification Proposal ID***(assigned by Secretariat)* |
| **SEMOpx** | **28 November 2017** | **Standard** | **Mod\_17\_17** |
| **Contact Details for Modification Proposal Originator** |
| **Name** | **Telephone number** | **Email address** |
| **Nigel Thomson** |  |  |
| **Modification Proposal Title** |
| **Recovery of Costs due to Invalid Ex-Ante Contracted Quantities in Imbalance Settlement** |
| **Documents affected***(delete as appropriate)* | **Section(s) Affected** | **Version number of T&SC or AP used in Drafting** |
| **T&SC Part B**  | **Section G** | **Version 20** |
| **Explanation of Proposed Change***(mandatory by originator)* |
| ***It is recommended to read the “Modification Proposal Justification” section of this proposal to provide the context for its submission prior to reading this section and subsequent sections of the proposed changes.***The changes proposed to the TSC seek to provide a workable solution to how specific low probability risks related to imbalances due to invalid Ex-Ante Market Contracted Quantities are mitigated in the I-SEM, given the interrelationship between the Ex-Ante Markets and Imbalance Settlement.The modification consists of changes to Section G of Part B of the Code to:1. Provide SEM NEMO’s time to recover costs from the relevant Exchange Member in order to pay Imbalance Settlement due to invalid Contracted Quantities.
2. Notify SEMO and Participants of the invalid Contracted Quantity issue[[1]](#footnote-1)
3. Withhold TSC payments to the relevant SEMO Participant subject to an invalid Contracted Quantity where the withholding of TSC payments will minimise the costs needing recovery for the invalid Contracted Quantity.
4. Use Balancing Market Posted Credit Cover from the relevant SEMO Participant to minimise the costs needing recovery for the invalid Contracted Quantity.[[2]](#footnote-2)
5. Utilise the short payment functions under the TSC until such time as costs have been recovered by the SEM NEMO.
6. Hold the SEM NEMO harmless for credit cover requirements related to the invalid Contracted Quantity related imbalance.
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| **Legal Drafting Change***(Clearly show proposed code change using* ***tracked*** *changes, if proposer fails to identify changes, please indicate best estimate of potential changes)* |
| The following provides the legal text changes needed to the TSC to accommodate the modification. ***In paragraph B.21.1.8, replace any words after the second reference to “limitation of liability” with the following:***“and without limiting sections F.21, F.22, G.2.7 or G.2.8.”***Insert the following words at the end of paragraph B.18.5.6(a):***“and/ or any Contracted Quantity submitted for the Participant under section F.2.2”***Insert a new section G.2.10 at the end of Section G.2, as follows:*****G.2.10 Invalid Contracted Quantities**G.2.10.1 For the purposes of this section G.2.10, a Contracted Quantity submitted by a SEM NEMO under paragraph F.2.2.1 (in its capacity as a Scheduling Agent) for a Participant is invalid where:1. the Contracted Quantity results from a trade in an Ex-Ante Market before the relevant Unit’s registration under this Code takes effect; or
2. the Contracted Quantity results from a trade in an Ex-Ante Market relating to a period during which a Trading Halt should have been in effect under the Market Rules; or
3. the Contracted Quantity results from a trade in an Ex-Ante Market relating to a period during which the relevant Unit is suspended from participation under this Code in accordance with section B.18.5.

G.2.10.2 Where a SEM NEMO considers that a Contracted Quantity is invalid, then the SEM NEMO may notify the Market Operator specifying:1. the Unit to which the invalid Contracted Quantity relates (called the “**specified Unit**” in this section G.2.10); and
2. the applicable invalid Contracted Quantity; and
3. the Imbalance Settlement Period to which the invalid Contracted Quantity relates; and
4. the reason why the Contracted Quantity is invalid; and
5. the steps that the SEM NEMO proposes to take to recover the cost the SEM NEMO incurs in relation to the invalid Contracted Quantity and the mechanisms that will be used to recover those costs under the Market Rules of the Ex Ante Market; and
6. the SEM NEMO’s best estimate of when those costs will be recovered under the Market Rules of the Ex Ante Market.

G.2.10.3 A notice under paragraph G.2.10.2 must be given before the relevant Payment In Due Date.G.2.10.4 As soon as practical after receiving a notice under paragraph G.2.10.2, the Market Operator shall publish the notice.G.2.10.5 Notwithstanding anything else in this Code, where the Market Operator receives a notice under paragraph G.2.10.2 in respect of a Contracted Quantity before the time determined in accordance with paragraph G.2.10.3:1. to the maximum extent permissible at law, the amount payable by the Market Operator to the Participant in respect of the specified Unit (called the “**Relevant Participant**”) under section G.2.5 on the relevant Payment In Due Date shall be reduced by an amount (called the “**Reassigned Amount**”) equal to the specified invalid Contracted Quantity multiplied by the Imbalance Settlement Price for the Imbalance Settlement Period to which the invalid Contracted Quantity relates; and
2. the amount payable by the relevant SEM NEMO to the Market Operator under section G.2.5 on the relevant Payment Out Due Date shall be reduced by the Reassigned Amount; and
3. to the extent that the Reassigned Amount is less than the unadjusted amount payable by the Market Operator to the Relevant Participant under section G.2.5 on the relevant Payment In Due Date (the difference between the two amounts is in this section referred to as the “**initial shortfall**”):
4. if the Relevant Participant has Posted Credit Cover as at the Payment In Due Date, the Market Operator shall make a Credit Call on the Relevant Participant’s Posted Credit Cover for payment of the lesser of the initial shortfall and the amount of the Posted Credit Cover (the lesser of those two amounts is in this section referred to as the “**draw-down amount**”) and, for the purpose of making such Credit Call on the Relevant Participant’s Posted Credit Cover:
	1. clause G.2.6.2 applies as if the draw-down amount was a “Shortfall” (and ignoring references to Agreed Procedure 15 when applying paragraph G.2.6.2); and
	2. the Relevant Participant shall be deemed to be in default of an obligation to pay the draw-down amount pursuant to this Code; and

 (ii) to the maximum extent permissible at law, the Market Operator shall be entitled to reduce payments to the other Participants under this Code on the relevant Payment Out Due Date by an aggregate amount (in this section called the “**remaining** **amount**”) equal to the initial shortfall less any sum drawn down as a result of the Credit Call made under paragraph G.2.10.5(c)(i), and in so doing, so far as practicable and *mutatis mutandis*, apply the provisions of paragraphs G.2.7.3, G.2.7.5 and G.2.7.7 as if the remaining amount was an Unsecured Bad Debt and an Unsecured Bad Energy Debt (and ignoring references to the Defaulting Participant(s), a Default and Default Interest when applying the provisions of paragraphs G.2.7.3, G.2.7.5 and G.2.7.7); and(iii) paragraph G.2.10.5(a) shall be reapplied on subsequent Payment Due Dates for the purpose of paragraph G.2.5.4(c) until the remaining amount has been recovered in full from the Relevant Participant in respect of the relevant Unit; and1. all Participants agree to any adjustments contemplated by this paragraph G.2.10.5 and that the payment of a reduced amount in place of the unadjusted amount in accordance with this paragraph G.2.10.5 does not constitute a breach or default of this Code on the part of the Market Operator or the SEM NEMO; and
2. despite the previous sub-paragraphs, when calculating the level of Required Credit Cover for the Relevant Participant and the relevant SEM NEMO, the Reassigned Amount shall be regarded as owed by the Relevant Participant and not the SEM NEMO.

G.2.10.6 Where a relevant SEM NEMO has provided a notice under paragraph G.2.10.2 to the Market Operator, thatSEM NEMO shall:1. take all steps available to it under the Market Rules of the Ex Ante Market or otherwise to recover the Reassigned Amount from the person whose trade in the Ex Ante Market gave rise (in whole or in part) to the invalid Contracted Quantity; and
2. where the SEM NEMO has appointed a separate clearing house to act as the central counterparty for the Ex Ante Market, use reasonable endeavours to procure that the clearing house takes all steps available to the clearing house under its Clearing Conditions or otherwise to recover the Reassigned Amount from the person whose trade in the Ex Ante Market gave rise (in whole or in part) to the invalid Contracted Quantity; and
3. pay to the Market Operator any amounts so recovered.

G.2.10.7 If: 1. because of the operation of paragraph G.2.10.5(c)(ii), a Participantdoes not receive the full amount that the Market Operator is otherwise required to pay the Participant in respect of any Billing Period (the amount not received by the Participant due to the operation of that paragraph being called a “**Reduction in Payment**”); and
2. either:
3. paragraph G.2.10.5(a) is reapplied in accordance with paragraph G.2.10.5(c)(iii) on a subsequent Payment Due Date and an amount is recovered from the Relevant Participant; or
4. the Market Operator is subsequently paid an amount under paragraph G.2.10.6 by the relevant SEM NEMO

in respect of the relevant invalid Contracted Quantity (in this section called the “**recovered amount**”), then, subject to paragraph G.2.10.8, that Participantis entitled to be reimbursed the amount of the Reduction in Payment it suffered. G.2.10.8 If the recovered amount is not sufficient to pay all Participantsthe Reduction in Payments they suffered in full, then the recovered amount is to be distributed amongst the applicable Participants pro rata according to the Reductions in Payment they suffered, with the process repeated each time to the extent that there is a recovered amount in respect of the same invalid Contracted Quantity until each Participant has been reimbursed in aggregate the amount of the Reduction in Payment it suffered. (it being acknowledged by each affected Participant under paragraph G.2.10.7 and this paragraph G.2.10.8 that there may not be sufficient recovered amounts to reimburse in aggregate the total amount of the Reduction in Payment suffered by it). G.2.10.9 Settlement Documents issued under Chapter G shall include an additional payment line item reflecting any reimbursement under paragraphs G.2.10.7 and G.2.10.8.***NEW DEFINITIONS (to be inserted in alphabetical order in the Glossary):***

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| **Clearing Conditions** | where a SEM NEMO has appointed a separate clearing house to act as the central counterparty for the Ex Ante Market the SEM NEMO operates, means the rules, code, procedures, terms and conditions under which the clearing house carries out that role. |
| **Ex-Ante Market** | means a day-ahead market or an intraday market operated by a SEM NEMO and includes the markets operated by EirGrid plc and SONI Limited (in their capacity as SEMOpx). |
| **Market Rules** | in respect of anEx-Ante Market:1. means therules, code, procedures, terms and conditions governing that market; and
2. where a separate clearing house has been appointed to act as the central counterparty for the Ex Ante Market, includes the Clearing Conditions.
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| **Payment In Due Date** | in respect of an invalid Contracted Quantity within the meaning of paragraph G.2.10.1, means the Payment Due Date for the purpose of sub-paragraph G.2.5.4(c) in respect of Settlement Documents covering the Imbalance Settlement Period to which the invalid Contracted Quantity relates. |
| **Payment Out Due Date** | in respect of an invalid Contracted Quantity within the meaning of paragraph G.2.10.1, means the Payment Due Date for the purpose of sub-paragraph G.2.5.4(d) in respect of Settlement Documents covering the Imbalance Settlement Period to which the invalid Contracted Quantity relates. |
| **Reassigned Amount** | in respect of an invalid Contracted Quantity within the meaning of paragraph G.2.10.1, has the meaning given in paragraph G.2.10.5(a). |
| **Relevant Participant** | in respect of an invalid Contracted Quantity within the meaning of paragraph G.2.10.1, has the meaning given in paragraph G.2.10.5(a). |

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| **Modification Proposal Justification***(Clearly state the reason for the Modification)* |
| **Why is the Modification being raised?**The design of the I-SEM includes a component related to Imbalance Settlement being based partly on Contracted Quantities agreed in Ex-Ante Markets. The consequences of any such Contracted Quantity being considered invalid by the Market Operator is an imbalance occurring against the relevant SEM NEMO under the Trading and Settlement Code - for the value of the Contracted Quantity at the Imbalance Price.During SEMOpx’s evaluation of financial risks associated the interrelationship between the Ex-Ante Markets and Imbalance Settlement there have been identified specific “scenarios” that could lead to this situation of Contracted Quantities being considered invalid in Imbalance Settlement. Although they have an extremely low probability of occurrence the impact in terms of financial costs needing recovery could be high.SEMOpx does not have the financial resources nor operating environment to cover this type of potential risk neither in the short term through working capital to finance the imbalance costs for imbalance settlement while the invalid Contracted Quantity costs are recovered, nor in the long term should the invalid Contract Quantity costs not be recovered. Therefore, mechanisms must be in place to mitigate against these risk scenarios and their impacts to ensure SEMOpx is not exposed to liabilities imposed by the Balancing Market that it is not able to take on.**How the Risk Eventuates**The specific scenarios identified, with an indication of their probability and impact, are provided below.

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| Scenario | Probability | Impact |
| Exchange Member trades in the Ex-Ante Markets before a Unit is effective in the Balancing Market | Extremely Low | High |
| Exchange Member trades in the Ex-Ante Markets while a Trading Halt should have been in effect. | Very Low | High |
| Exchange Member trades in the Ex-Ante Markets while a Suspension of the relevant Unit from the Balancing Market is in effect. | Extremely Low | High |

**Probability of the Risk Occurring**To illustrate the extremely low probability of this event occurring, the diagram below shows the sequence of events that would need to occur in order for this risk to eventuate.**Impact if the Risk Eventuates**While the probability of the scenario occurring is extremely low the impact of such an event could be significant. Although it is difficult to quantify the monetary impact of the scenarios – as there is a great deal of variability and lack of historical data in most cases. However, examples of the costs that could need recovery are illustrated below.Please note that:* These exposures are only expected for one auction and trading day as measures would be implemented immediately to rectify the issue and avoid further invalid Contracted Quantities for subsequent auctions.
* The figures assume that the Ex-Ante payments for the invalid Contracted Quantity has not been able to be withheld - which would reduce the costs needing recovery to just the Contract Quantity x the difference in Imbalance and Ex-Ante prices.

**Implications for Imbalance Settlement**To recover the costs associated with any of the invalid Contracted Quantity scenario, a SEM NEMO would need to obtain the relevant costs in order to pay the imbalance. The processes to recover these costs may not be able to be completed in sufficient time to meet the required payment deadlines for Imbalance Settlement.In addition, although a SEM NEMO will utilise several mechanisms in order to recover the invalid Contracted Quantity costs, there is still an extremely low probability that the costs are never fully recovered and therefore the imbalance cannot be fully repaid by SEM NEMO in Imbalance Settlement.This provides two key issues of:1. Who funds the working capital of the imbalance under Imbalance Settlement until the costs of the invalid Contracted Quantity are recovered?; and
2. Who ultimately, if all other measures fail, bears the cost of any remaining costs related to the invalid Contracted Quantity?

**Who funds the Working Capital to cover the Imbalance prior to Recovery?**Based on the financial and operating model proposed for SEMOpx under regulatory requirements, the service will operate on a cost pass through model with no allowance for the costs of working capital. Therefore, SEMOpx is not in a position to provide working capital to fund an imbalance due to invalid Contracted Quantities.Therefore the only plausible solution is that a SEM NEMO can notify the Market Operator of a delay in recovering the costs associated with the invalid Contracted Quantity and the Market Operator in acknowledging this delay, hold SEM NEMO harmless and short pay the relevant recipients of the imbalance payment until such time as the costs can be recovered by SEM NEMO. **If all else fails, who bears any residual costs of the invalid Contracted Quantity?**In considering the bearing of residual costs, it should be noted that prior to this ultimate bearing of invalid Contract Quantity costs there will be a number of mitigation measures that will be looked at to be implemented in order to minimise the likelihood of this bad debt occurring. These mitigation measures mean that in addition to the event being extremely unlikely to occur, the chances of the costs not being recovered, using the mitigation measures below, are extremely low.**Mitigation Measures to Minimise Residual Costs**The potential measures to mitigate the bearing of invalid Contracted Quantities could include:1. SEM NEMO withholding payment to the Exchange Member for the value of the invalid Contracted Quantities therefore minimising the costs needing recovery.
2. SEMO to withhold any payments for the relevant Units in Imbalance Settlement to minimise the costs needing recovery.
3. SEMO to use Posted Credit Cover for the relevant Units in Imbalance Settlement to minimise the costs needing recovery.
4. SEM NEMO to charge the Exchange Member that caused the invalid Contracted Quantities through trading in the Ex-Ante Markets, when not authorised to do so.
5. [[3]](#footnote-4)Where the issue can be attributed to SEM NEMO’s service providers, recovery of costs through liability provisions.
6. SEM NEMO to charge all other Exchange Members where the costs cannot be recovered from the Exchange Member or the Default Fund.

Thus, in order for the bad debt to ultimately crystalize, all the mitigation and recover of cost measures would have to have failed. As outlined in the diagram below.**Other Mitigation Measures that were Dispelled**There were also other measures considered to mitigate the impacts of these invalid Contracted Quantity scenarios. However, these have not been included as they are seen as inappropriate due to one or more of the following: they result in additional and considerable upfront and continuing costs for Exchange Members to cover a risk that has extremely low probability, the solution may cause major issues with the ongoing viability of the Ex-Ante Markets, or they are not feasible for implementation in the timeframes before I-SEM go-live. The measures that were considered, but dispelled were:1. Imposing significant additional collateral requirements on all Exchange Members to cover this risk scenario
2. Taking out insurance against these scenarios
3. Increasing Exchange fees upfront to cover this potential risk
4. Increasing Exchange fees after the event occurs to cover the realised residual costs.

**Proposed Approach for Residual Costs**Based on the financial and operating model proposed for SEMOpx under regulatory requirements, SEMOpx is not in a position to ultimately backstop the invalid Contracted Quantity costs should they not be recovered by other mitigation measures.Therefore the only plausible solution is that a SEM NEMO could notify the SEMO that the costs of invalid Contracted Quantity cannot be fully recovered and any unrecovered costs must be maintained as a bad debt by SEMO Participants. |
| **Code Objectives Furthered***(State the Code Objectives the Proposal furthers, see Section A of T&SC for Code Objectives)* |
| This Modification proposal aims to further the Code Objectives under TSC Section A.2.1.4, specifically the elements shown in bold below.(b) to **facilitate the efficient, economic and coordinated operation**, administrationand development of the Single Electricity Market **in a financially secure****manner;****(c)** to **facilitate the participation of electricity undertakings engaged in the generation, supply or sale of electricity** in the trading arrangements under the Single Electricity Market;(e) to **provide transparency in the operation** of the Single Electricity Market;(g) to **promote the short-term and long-term interests of consumers of electricity on the island of Ireland with respect to price**, quality, reliability, and security of supply of electricity.  |
| **Implication of not implementing the Modification Proposal***(State the possible outcomes should the Modification Proposal not be implemented)* |
| The implications of not implementing this modification proposal is that liability clauses related to the SEMOpx Rules will not be able to be agreed and Exchange Members will not be willing, without these clauses known, to sign the Exchange Member Agreement to facilitate trading in the I-SEM Ex-Ante Markets. |
| **Working Group***(State if Working Group considered necessary to develop proposal)* | **Impacts***(Indicate the impacts on systems, resources, processes and/or procedures; also indicate impacts on any other Market Code such as Capacity Marker Code, Grid Code, Exchange Rules etc.)* |
| Given: the limited time available, in order to provide clarity and certainty to Exchange Members and Participants about the recovery of costs related to invalid Contracted Quantities, it is proposed that the focus be on using this proposal as a basis for the final modification with any amendments being made to the proposal rather considering a number of alternatives from scratch which may take considerably more time, effort and may jeopardize the readiness of the market for I-SEM go-live. | The outcome of this modification proposal will have implications on SEM NEMO Rules. |
| ***Please return this form to Secretariat by email to*** ***modifications@sem-o.com*** |

**Notes on completing Modification Proposal Form:**

1. **If a person submits a Modification Proposal on behalf of another person, that person who proposes the material of the change should be identified on the Modification Proposal Form as the Modification Proposal Originator.**
2. **Any person raising a Modification Proposal shall ensure that their proposal is clear and substantiated with the appropriate detail including the way in which it furthers the Code Objectives to enable it to be fully considered by the Modifications Committee.**
3. **Each Modification Proposal will include a draft text of the proposed Modification to the Code unless, if raising a Provisional Modification Proposal whereby legal drafting text is not imperative.**
4. **For the purposes of this Modification Proposal Form, the following terms shall have the following meanings:**

**Agreed Procedure(s): means the detailed procedures to be followed by Parties in performing their obligations and functions under the Code as listed in either Part A or Part B Appendix D “List of Agreed Procedures”. The Proposer will need to specify whether the Agreed Procedure to modify refers to Part A, Part B or both.**

**T&SC / Code: means the Trading and Settlement Code for the Single Electricity Market. The Proposer will also need to specify whether all Part A, Part B, Part C of the Code or a subset of these, are affected by the proposed Modification;**

**Modification Proposal: means the proposal to modify the Code as set out in the attached form**

**Derivative Work: means any text or work which incorporates or contains all or part of the Modification Proposal or any adaptation, abridgement, expansion or other modification of the Modification Proposal**

**The terms “Market Operator”, “Modifications Committee” and “Regulatory Authorities” shall have the meanings assigned to those terms in the Code.**

**In consideration for the right to submit, and have the Modification Proposal assessed in accordance with the terms of Section 2 of Part A or Chapter B of Part B of the Code (and Part A Agreed Procedure 12 or Part B Agreed Procedure 12) , which I have read and understand, I agree as follows:**

**1. I hereby grant a worldwide, perpetual, royalty-free, non-exclusive licence:**

* 1. **to the Market Operator and the Regulatory Authorities to publish and/or distribute the Modification Proposal for free and unrestricted access;**
	2. **to the Regulatory Authorities, the Modifications Committee and each member of the Modifications Committee to amend, adapt, combine, abridge, expand or otherwise modify the Modification Proposal at their sole discretion for the purpose of developing the Modification Proposal in accordance with the Code;**
	3. **to the Market Operator and the Regulatory Authorities to incorporate the Modification Proposal into the Code;**

**1.4 to all Parties to the Code and the Regulatory Authorities to use, reproduce and distribute the Modification Proposal, whether as part of the Code or otherwise, for any purpose arising out of or in connection with the Code.**

**2. The licences set out in clause 1 shall equally apply to any Derivative Works.**

**3. I hereby waive in favour of the Parties to the Code and the Regulatory Authorities any and all moral rights I may have arising out of or in connection with the Modification Proposal or any Derivative Works.**

**4. I hereby warrant that, except where expressly indicated otherwise, I am the owner of the copyright and any other intellectual property and proprietary rights in the Modification Proposal and, where not the owner, I have the requisite permissions to grant the rights set out in this form.**

**5. I hereby acknowledge that the Modification Proposal may be rejected by the Modifications Committee and/or the Regulatory Authorities and that there is no guarantee that my Modification Proposal will be incorporated into the Code.**

1. Included based on suggestion in Participant feedback received [↑](#footnote-ref-1)
2. Included based on suggestion in Participant feedback received [↑](#footnote-ref-2)
3. Removed based on Participant feedback received [↑](#footnote-ref-4)