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8th June 2022

RE: Consultation on changes to reduce collateral requirements in the balancing market, SEM-22-024

Dear TSC Team and Karen,

Bord Gáis Energy (**BGE**) welcomes the opportunity to respond to this consultation on proposed changes to reduce collateral requirements in the balancing market (the "**consultation**").

In principle, BGE supports measures that can be taken to help address the high collateral requirements that participants in SEM face today. It is critical however that such measures are proportionate and fair such that all participants are on a level playing field when it comes to rules around posting collateral and that any risks created by the potential exit of a participant do not unfairly burden remaining participants to the ultimate detriment of end-consumers.

From a consumer cost exposure perspective our concern with the proposal to reduce the collateral required from participants in the Balancing Market (**BM**) centres on the risks of potential bad debt that could arise should the regulatory authorities (**RAs**) for example take longer than 5 days to make their decision on issuing a supplier of last resort (**SoLR**) direction. In this situation the bad debt accrued by the exiting supplier would be levied on remaining market participants, raising the cost of doing business for those participants with possible negative impacts for end-consumers. We believe however that this key risk could be mitigated by solutions including:

i. The insertion into the Trading and Settlement Code of provision(s) that assure market participants that the RAs must meet or at least exercise best endeavors to achieve the 5 day-deadline, and
ii. An insertion into the Trading and Settlement Code to the effect that if the RAs do not meet the 5-day deadline then the SEMO contingency fund will in the first instance be utilised to cover bad debt accruing on foot of exceeding the 5-day limit, and/ or
iii. SEMO could obtain a letter of credit to cover themselves against the incremental risk that the RAs' proposed change to the market design is introducing for participants that may be left with a bad debt accrued by an exiting participant.

   Options (i) and (ii) or (i) and (iii) in our view need to form part of the final decision in order to optimally protect consumers against future bad debt risk arising from the proposed market rule changes in this consultation. Please see answer 2 below for more details on this proposal.

We have also outlined below our views on the remaining questions in the consultation although our answers are somewhat constrained by being unable to comment on the internal workings of banks or other market participants.

Q1. Do you agree with the SEM Committee's proposals to amend the Single Suspension Delay Period to 5 days and thereby reduce the Undefined Exposure Period to 7 days?

Yes, we support a reduction in the Undefined Exposure Period (UEP) if the new potential risk this market design change presents is borne by the RAs and/ or SEMO. Reducing the cost of collateral should help maintain suppliers' competitiveness in the market for the ultimate benefit of end consumers. Reduced collateral requirements could also be seen as reducing barriers to entry for suppliers though we note in this regard that pursuant to the recent RePowerEU publication, minimum hedging requirements for suppliers are being considered at least on an EU level. BGE believes that such considerations will be important to achieving a balance between reducing collateral requirements while ensuring that suppliers (be they new entrants or existing participants) operate prudently in the market. Prudent utility practice is key to ensuring the longevity of market participants and mitigating the risk of unexpected market exit which can be detrimental for competition and consumers.

As discussed on page 1 above, BGE is concerned around the bad debt risk that could arise if the RAs' decision on an SoLR event took longer than 5 days. The tradeoff between this increased risk of bad debt vs. the reduced collateral burden will only be acceptable if measures are adopted that protect against remaining market participants being wholly responsible for funding the bad debt of a supplier that exits. We believe that such measures are necessary to protect against consumers facing a currently unquantifiable risk of such an outcome materialising on foot of the market design change proposed in this consultation. Please see answer 2.

Q2. Do you agree that an increased risk of bad debt in the balancing market is an acceptable trade-off when weighed against the reduced collateral burden on all Participants in the market on an ongoing basis?

As outlined above, BGE has considerable concerns around the risks to remaining participants and in turn consumers who could face millions of euros in shared bad debt exposure if the RAs miss the newly determined 5-day deadline for deciding on whether a market participant should exit the market.

It is accepted practice in general risk management that the risk should sit with the entity that can best control it. In this instance, we believe that the RAs are the entities that can control whether bad debt on the part of a participant that must exit will arise. It would be possible in our view to mitigate this longer-term risk to consumers (of the 5-day SoLR decision-making window being exceeded) in a number of ways including:

i. If the RAs could reasonably assure market participants of their planned adherence to the 5-day limit. Such an assurance could be given for example by inserting a provision into section G.12 of the Trading and Settlement Code or into Agreed Procedure 9 (**AP9**) outlining that the RAs are time-bound to 5 days to make the decision (or will at least exercise best endeavours to meet the timeline), and;
ii. The SEMO contingency fund could be referred to, in either of the G.12 or AP9 Trading and Settlement Code provisions, to outline that in instances where the 5 days has been exceeded any bad debt accrued by an exiting participant will be covered by the fund, and/ or;
iii. SEMO could procure a letter of credit to cover those instances where the RAs may exceed their 5-day limit in order to cover the bad debt accrued by a participant that must exit.

BGE believes that at least either (i) and (ii) or (i) and (iii) above should be incorporated into the final decision on this consultation in order to provide suppliers with the benefit of reduced collateral costs but also, as importantly, to protect consumers against the ultimate bad debt risk that could accrue if the reduction in the Single Suspension Delay Period (from 7 to 5 days) proves to be too tight for the RAs at any point in future.

Q.3: In your view, what are the reasons why many Participants in the balancing market are posting extra Credit Cover, significantly over and above their Required Credit Cover?

BGE is not in a position to comment on other market participants' approaches to posting credit cover in the balancing market, but we provide our view on the matter and our own processes in answer to question 4 below.

Q.4: In your view, are the approval times for Letters of Credit causing Participants to post extra Credit Cover as "headroom" as they believe they may find it difficult to meet the timelines of a Credit Cover Increase Notice (CCIN) with a Letter of Credit?

Yes. In our experience increasing the value of a letter of credit (**LC**) will generally take 2-3 weeks, or likely longer if a new LC is being raised. BGE therefore believes it is often prudent to maintain a level of "headroom" between Required Credit Cover and the value of the LC to reduce the likelihood of the requirement to post cash to meet a Credit Cover Increase Notice.

Q.5: What are your views on the approval times for Letters of Credit generally? Are there any changes that could be made to the current approval processes that would allow Letters of Credit to be approved more quickly (bearing in mind that Letters of Credit must meet the conditions set out in Agreed Procedure 9)?

BGE is of the view that approval times for raising or amending letters of credit are based on the internal controls and processes in place at both the issuing banks and at the businesses being supported. Expediting the timelines of banks, if it could be agreed, would potentially be at the expense of due diligence which would not benefit industry and potentially raises more risk for consumers. Banks usually assess each company based on their creditworthiness and assessment of items such as credit ratings, key ratios and market environment. The banks then decide how much they are willing to insure and at what cost – their primary objective is to accurately price the risk they are taking on. We do not believe that credit providers/ banks issuing letters of credit or collateral have any incentive to reduce timelines and ultimately for SEM those timelines currently work to protect consumers against the risk of bad debt.

I hope you find the above suggestions and comments helpful. Please do not hesitate to contact me should you wish to discuss any aspect of the above.

Yours sincerely,

Julie-Anne Hannon
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Bord Gáis Energy

{By email}