

Single Electricity Market

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| Final REcommendation ReportMod\_02\_17 : Unsecured Bad Energy Debt and Unsecured Bad Capacity Debt timelines 25 August 2017 |

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Document History

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| 1.0 | 10/08/2017 | Modifications Committee Secretariat | Issued to Modifications Committee for review and approval |
| 2.0 | 25/08/2017 | Modifications Committee Secretariat | Issued to RA’s for Final Decision |

Reference Documents

|  |
| --- |
| **Document Name** |
| [Trading and Settlement Code](http://semopub/MarketDevelopment/MarketRules/TSC.docx) |
| [Agreed Procedure 15](http://www.sem-o.com/MarketDevelopment/MarketRules/AP15.docx) |
| [Modification Proposal](http://semopub/MarketDevelopment/ModificationDocuments/Unsecured%20Bad%20Debt%20Modification%20Proposal_Version_1.0.docx) |
| [Modification Proposal Presentation – Meeting 72](http://semopub/MarketDevelopment/ModificationDocuments/Mod_02_17%20Unsecured%20Bad%20Debt.pdf) |
| [Meeting 72 Summary Responses](http://semopub/MarketDevelopment/ModificationDocuments/Summary%20of%20Actions%20from%20MO%20on%20Unsecured%20Bad%20Debt%20Mod_02_17.pdf) |
| [Modification Proposal Presentation – Meeting 73](http://semopub/MarketDevelopment/ModificationDocuments/Mod_02_17%20Unsecured%20Bad%20Debt_meeting%2073.pdf) |
| [Meeting 73 Summary Responses](http://semopub/MarketDevelopment/ModificationDocuments/Summary%20of%20additional%20Actions%20and%20responses%20from%20MO%20on%20Unsecured%20Bad%20Debt%20Mod_02_17.docx) |

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# MODIFICATIONS COMMITTEE RECOMMENDATION

## Recommended for rejection

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| **Recommended for Rejection**  |
| Kevin Hannafin-Chair | Generator Member | Reject |
| Brian Mongan | Generator Member | Reject |
| Conor Powell | Supplier Member | Reject |
| William Steele | Supplier Member | Reject |
| Eamonn O’Donoghue | Interconnector Member | Reject |
| David Connolly | Generator Member | Reject |
| Julie-Anne Hannon - Vice Chair | Supplier Member  | Approve |
| Clive Bowers | Generator Alternate | Approve |
| Jim Wynne | Supplier Member | Approve |

# Background

This Modification Proposal was initially raised with the following title: Unsecured Bad Energy Debt and Unsecured Bad Capacity Debt timeline’s.

It was received by the secretariat on the 25th January 2017.

The Modification Proposer [presented](http://semopub/MarketDevelopment/ModificationDocuments/Mod_02_17%20Unsecured%20Bad%20Debt.pdf) the Modification to the SEM Committee at Meeting 72. The presentation detailed the current Unsecured Bad Debt timelines, proposed Unsecured Bad Debt timelines, the Justifications for the Modification Proposal and the tracked changes to the Trading & Settlement Code and Agreed Procedure 15.

A summary of action was received from the Market Operator by the secretariat regarding issue and actions taken from Meeting 72. [This](http://semopub/MarketDevelopment/ModificationDocuments/Summary%20of%20Actions%20from%20MO%20on%20Unsecured%20Bad%20Debt%20Mod_02_17.pdf) was published to the SEM Modifications Committee.

The Modification proposal was further discussed at Meeting 73. A [second presentation](http://semopub/MarketDevelopment/ModificationDocuments/Mod_02_17%20Unsecured%20Bad%20Debt_meeting%2073.pdf) regarding the proposed Unsecured Bad Debt timelines including clarification of the current Trading & Settlement Code timelines was presented to the SEM Modifications Committee.

A summary of action was received from the Market Operator by the secretariat regarding issue and actions taken from Meeting 73. [This](http://semopub/MarketDevelopment/ModificationDocuments/Summary%20of%20additional%20Actions%20and%20responses%20from%20MO%20on%20Unsecured%20Bad%20Debt%20Mod_02_17.docx) was published to the SEM Modifications committee.

# PURPOSE OF PROPOSED MODIFICATION

**3A.) justification of Modification**

The Market Operator has recently reviewed its internal processes including Unsecured Bad Debt. This review highlighted that under the current Trading & Settlement Code timelines (Section 6.50 & Agreed Procedure 15), System Functionality and external timelines, the Market Operator would be unable to complete the Bad Debt smearing process within the timelines set out in the Trading & Settlement Code and thereby be in breach. The current timeline is to deliver the issuing of Debit Notes and net payment of Self Billing Invoices by 17:00 4 Working Days after the date of the Self Billing Invoice.

Justification for this modification is due to the below points:

* Bad Debt smearing, once implemented within the SEM Central Market System cannot be interrupted or cancelled.
* Under the current timelines, the functionality of the Central Market System, the Market Operator would be unable to deliver the Bad Debt smearing process given the current 14:30 cut off for Banking Payment Approvals.
* Potentially, all Settlement Runs relating to Energy and Capacity Markets may be processed as Unsecured Bad Debt due to Participant Defaults .
* Large volume of Banking Payments requiring Senior Management Approval under current tight timeframes.
* Meticulous Internal checks and approvals.
* Complex process within the Market Operator.
* Potential disruption of Participants internal processes under stressed timeframes.

Given the financial implications and the processing of Unsecured Bad Debt under tight timelines, the Market Operator feels that this Modification if passed would release the pressures of implementing this protracted process whereby the all necessary diligence, approvals and banking cut off timelines could be met.

If passed, this modification would be implemented within the current T&SC (Part A) for the current SEM market.

The Market Operator will review the Technical specifications and requirements regarding Unsecured Bad Debt within the I-SEM Market.

**3B.) Impact of not Implementing a Solution**

Under the current timelines and the financial implications, the Market Operator explored alternative options regarding this modification, though the Market Operator felt that the recommendation detailed above would provide an efficient end to end process for the Bad Debt smearing process, a direct result of implementing Unsecured Bad Debt within the SEM. These include:-

* System Functionality
* External Banking approval timeline
* SEMO Overdraft facility
* Publication timelines of Debit Note in event of Unsecured Debt
* Reducing Time to Remedy

The impacts of not implementing the Modification Proposed, is the Market Operator would be in breach of the Trade & Settlement Code. This was stressed by the MO member within Meeting 74.

As per the justifications for the Modification Proposal, the Market Operator would not be able to meet the current timelines in the event of calling Unsecured Bad Debt.

**3c.) Impact on Code Objectives**

This modification aims to further the following code objectives:

Section 1.3:

To facilitate the efficient, economic and coordinated operation, administration and development of the Single Electricity Market in a financially secure manner;

1. **Assessment of Alternatives**

The [summary](http://semopub/MarketDevelopment/ModificationDocuments/Summary%20of%20Actions%20from%20MO%20on%20Unsecured%20Bad%20Debt%20Mod_02_17.pdf) of actions and responses received by the secretariat in response of Meeting 72, detail reasoning behind the alternative options explored by the Market Operator.

# Working Group and/or Consultation

N/A

# impact on systems and resources

System Impacts:

* There are no system impacts as a result of the Modification.

Resource Impacts:

* There are no resource impacts as a result of the Modification on the Market Operator, though there may be potential resourcing impacts on Participants.

SEM Impacts

* Participant’s financial position to be accessed on an Individual basis.
* SEM Creditors, payment of Self Billing Invoices less Debit Note would be by 17:00 5WD after the date of the Invoice.
* Reduce potential instances in where by Unsecured Bad Debt may be implemented.

All processes and procedures Unsecured Bad Debt as detailed above

# Impact on other Codes/Documents

N/A

# MODIFICATION COMMITTEE VIEWS

## Meeting  **72 – 7 february 2017**

Proposer delivered a [presentation](http://semopub/MarketDevelopment/ModificationDocuments/Mod_02_17%20Unsecured%20Bad%20Debt.pdf) relating to Unsecured Bad Debt. The presentation highlighted the issues surrounding the current timelines as per Trading & Settlement Code (T&SC) V.18 and the Central Market System constraints in the event of Unsecured Bad Debt. As per section 6.55 of the T&SC, if a shortfall (Energy / Capacity) is not paid in full by 12:00 next Working Day after the Invoice Due Date, the amount of the Shortfall shall become an Unsecured Bad Debt. In the event of Unsecured Bad Debt, the Market Operator shall be subject to the calculation of an adjustment by a reduction in the amount payable to each affected SEM Creditor pro-rated and issue a Debit Note for the reduced amount, pay Self Billing Invoices net any Debit Note by 17:00, 4 Working Days after the date of the Self Billing Invoice.

The modification proposes to adjust the above timelines, only in the event of Unsecured Bad Debt to 17:00, 5 Working Days after the date of the Self Billing Invoice providing the Market Operator sufficient time to complete their internal processes efficiently as a result of Unsecured Bad Debt.

The current timelines and code obligations on the Market Operator are unrealistic due to external timelines and Central Market System constraints. Detailed within the presentation, the proposer highlighted further justification for the modification including the implications of not implementing this modification proposal and two alternative proposals considered.

Chair thanked the proposer for the presentation and invited questions from the committee. Supplier Member enquired how the submissions of Settlement Reallocation Agreements are treated within the calculation of Unsecured Bad Debt. Seeking clarification, if a SEM creditor pre Unsecured Bad Debt with the inclusion of Settlement Reallocation Agreements could ultimately become a SEM Debtor. MO Member suggested that this was a possibility if the calculation was not based on the Invoiced Amount, though was unsure and would confirm this after further internal investigation.

Supplier member enquired as to whether the 2.30pm cut off period was an internal or external timeline. RA Alternate asked if this timeline could be moved. MO Member advised that this was an external timeline and the likelihood of this being changed would be very slim, including that SEMO finance have an agreed mandate with the SEM bank which he could not comment on. The SEM bank requires payments to be approved by this cut off period to process the settlement and banking obligations as per Trade & Settlement Code timelines. The MO Member advised that given the current timelines for calling Unsecured Bad Debt and the Central Market System processing times, the Market Operator would not be able to meet the 2.30pm approval cut off period. In the event where Unsecured Bad Debt over 3 settlement run ( Initial, M+4 & M+13), parallel processing would take place and increase the Central Market System processing times in the calculation of Debit Notes.

Generator Member asked what time a generator member will be informed of Unsecured Bad Debt event under this proposal. Proposer advised that it would be 12.00pm 4 Working Days, after the Date of the Self Billing Invoice as soon as the Unsecured Bad Debt was being called upon. MO Member advised that in the event of Unsecured Bad Debt, the Market Operator would communicate via market message as soon as possible after 12:00.

As per presentation, the proposer detailed that once the Unsecured Bad Debt has been called and implemented within the Central Market System, the process cannot be interrupted or cancelled via system or manual intervention. Therefore the settlement of the affected Billing Week cannot be rolled back to original settlement status.

Generator Member advised that they already carry the risk of Unsecured Bad Debt and raised concerns that not only this, with the introduction of the modification they would then have to carry a 2nd risk of not knowing what funds they would be receiving in the event of Unsecured Bade Debt including any reductions until 17:00, 5 Working Days after the date of the Self Billing Invoice negatively affecting their cash flow. MO Member advised that those risks were currently being carried.

Generator Member posed the reality that if 80% of Generator’s Invoices is in SRA’s to Suppliers, then does that mean that only two or three generators are carrying this risk. Another Generator Member felt that this could be discriminatory. Observer suggested the indicative amounts could be assessed.

Discussion ensued in relation to the process of self billing invoice and waiting to go to the bank. Generator Member advised that a debit note must be completed as per the current Trading and Settlement Code. MO Member advised that in the case of the Unsecured Bad Debt smearing process the Self Billing Invoice has to be adjusted therefore cannot be paid as originally issued. Supplier Member stated that the issue is who manages the shortfall.MO Member advised that due to the current Central Market System constraints and external Banking constraints, the current timelines within the Trade & Settlement Code are not manageable thus triggering the urgency for the modification.

Supplier Member suggested could the calculation and net payment of Debit Notes to be flagged in the SBI affected and be deferred and smeared into following week Settlement. MO Member advised that SEMO cannot manage capital risk. All funds are to be received by the Market Operator before Self Billing Invoices can be paid. Supplier Member suggested an Option, in the event of Unsecured Bad Debt SEMO could be able to put in place an overdraft facility to ensure that all funds would be received by the 12:00, 4 Working Days after the Date of the Self Billing Invoice. RA Member advised that this may not be something that SEMO can drawdown on as previously investigated.

Supplier Member stated that this is different from previously open ended long term overdraft facility because it would be limited to a week only and expected to be only for extreme circumstances and limited amount. MO advised that this could not be guaranteed, however the question would be presented to the Finance Department again to see if this represented a possibility. The option of moving the 2.30pm deadline needs investigated. Other Generator Members voiced agreement with the concern regarding delay in payments and asked if there were other options. MO Member advised at this time, the likelihood was that there were no other options, other than the alternative options detailed within the proposer’s presentation, i.e. moving the deadline for payments out to Self Billing Invoices or reducing the timelines currently available to Suppliers to remedy on their default.

MO Member advised that if the timelines were changed for when the Market Operator would call Unsecured Bad Debt this moves the risk to suppliers and potentially increases the risk of Unsecured Bad Debt actually happening. To date the process has never been called yet, but was very close to being called a number of times, and this was prevented by the time of remedy. Supplier Members expressed concern. Supplier Member advised they would take this discussion back to their organisation and review the implications.

Generator Member asked how much of the required process time is system driven. Proposer advised that it took 2 hours to run a settlement batch. This time has potentially increased due to the number of units in the market, however no exact details exists of the original tests done at SEM go live. Generator asked when in the process it has been realised that there is a problem. MO Member confirmed this was when MO was very close to having to calculate a debit note.

DSU Member enquired as to what systems are being used and could the avenue be explored regarding the improvements to the Central Market System to reduce processing times. MO Member and Proposer advised that they would review the database for any potential efficiency to be achieved by indexing, archiving or other processes not requiring vendor intervention or system changes. Chair asked if such an event has ever happened. MO Member advised that such an event was very recently close to happening bringing this issue to light. Generator Member voiced the suggestion that this was a resource issue, whether that be people or systems.

Another Generator Member said that Generators are still exposed today to this unknown if the MO can’t clearly operate within the deadlines imposed by the T&SC. Any System changes will likely carry at least 9 months lead up to implementation where this risk would be still in place and that it would be preferable to have certainty about being paid a day late that not knowing when this would happen at all. The question was raised as to whether it would be possible to give an indication of the revised amount to be paid to Generator as early as possible prior to the 17:00 deadline proposed by the modification.

Alternative suggestions made by the committee were as below;

* Improved System functionality to reduce processing timelines
* Change of external Banking approval cut off deadlines of 14:30
* Investigating SEMO Overdraft facility
* SU to investigate and comment back on potentially reducing the available time to remedy
* It was also requested if possible to investigate Debit Note being issued in advance of the 17:00 payment to give timely information to GU about the amount due to them.

MO Member proposed reviewing the process internally and to take away the various points raised and query. This information will then be communicated to the members for them to review. A conference call with then be facilitated.

## Meeting  **73 – 6 april 2017**

MO Member apologised for the delay in the provision of the paper issued the day before. MO Member also provided a [summary presentation](http://semopub/MarketDevelopment/ModificationDocuments/Mod_02_17%20Unsecured%20Bad%20Debt_meeting%2073.pdf). MO Member advised that there were no identifiable actions that could be taken to improve the process timelines. It was explained that a number of changes took place after the intra day trading project to improve the manual processes.

MO Member addressed each area proposed by the Panel in Meeting 72 for reviewing the timing deadlines within this process, but advised that there was no scope for further efficiencies or improvements as outlined in the document circulate prior to the meeting.

The banking deadline is a stringent timeline that could not be moved while internal processing could not be completed before that to allow for same day payment in the event of Unsecured Bad Debt. This is in particular relevant for Sterling Payments.

The issue of SEMO having an overdraft facility to cope in such circumstances was addressed again. MO Member advised that an overdraft facility was not viable for SEMO. Such an arrangement was not provided for in the current terms and there is no mechanism for this function.

MO Member explained that version 1 of the Modification had been developed quickly because raised as urgent modification. In this haste there was a lack of clarity in terms of provisions of the Coded referenced in the Mod. MO Member advised that legal interpretation was sought and that determined that the code already has appropriate rules in place though they may not be explicit. Sections 6.57 and 6.58 of Trading and Settlement Code (T&SC) in particular are the key provisions at this regard.

MO Member reiterated that SEMO has no funding mechanism and that the market is based on the system of getting the money in before paying the money out. Two documents referenced in the above provisions were the Debit Note and the Debit Note Excess. Question was raised by supplier member at previous meeting 72: could a generator find himself as a debtor. MO Member responded that the calculation was not done on the invoice totals, as initially advised in meeting 72, but on the settlement payments/charges therefore prior to inclusion of SRAs. This means that there could be scenario where a Generator with SRA could now find itself in a situation of owning money to the Market. As the two documents referred to in 6.57 and 6.58 are produced as part of the same process the same market principle of money in before money out should apply.

MO Member advised that this would result in payments to be delayed by at least 2 days after the Debit Note is issued in the event of Debit Note Excess. MO Member reiterated that otherwise the market had no mechanism to pay for the shortfall.

Observer advised that they disagreed with the interpretation of sections 6.57 and 6.58. Observer queried if a supplier doesn’t pay by 12pm Wednesday then the credit cover should be drawn down – shouldn’t the credit cover be enough? MO Clarified that this is the case, however where credit cover is insufficient, they still have until 12 pm the next working day to rectify. After that time and only in those circumstances it becomes a bad debt.

Observer noted that some generators have Settlement Reallocation Agreements (SRA’s) and the scenario of Debit Note Excess will only occur if a generator has submitted SRAs to a level greater than their Self Billing Invoice minus the bad debt reduction. Observer continued that Unsecured Bad Debt and Debit Note Excess should both be smeared via an iterative loop which runs until there is are no longer any Excess Participants and the programming code should be able to reverse the out the Unsecured Bad Debt in case a payment is then received. Observer referenced section 6.58 of T&SC claiming that with SEMO interpretation, SEMO is withholding moneys that people are entitled to. Observer believes that what is happening in practice is contrary to the T&SC and that it does not explicitly state anywhere that no payments should be made until funds in relation to Debit Note Excess have been received.

Supplier Member advised that they agreed with the logical approach advocated by the Observer. The likelihood of this issue in I-SEM was raised. MO Member advised that under the new proposals the reallocation agreement is different. Generator Member advised that he agreed with the comments raised by the Observer and claimed it fundamentally unacceptable for SEMO to defer all payments in this scenario as section 6.57 doesn’t restrict timelines. MO Member commented that the original issue still remains, the fact that there is not sufficient time to process the payments if the shortfall has not been addressed by Suppliers within the allowed timelines.

Supplier Member commented in every previous bad debt circumstance, payment came in overnight or first thing the next morning and has been avoided due to the time to remedy being 12.00pm. If the timelines were reduced to 17:00 same day in this scenario it is the supplier that carries the risks of a shorter window for time to remedy and an Unsecured Bad Debt would be called more often affecting Generators in turn. Generator member queried if this timing was a banking issue where by suppliers were not making payments in good time for them not to be paid by 12.00 deadline on the third working day. Supplier member advised that this only occurred in exceptional circumstances. MO Member was asked off frequency of bad debt situations occurring. It was responded that there were limited cases of near missed events but the triggers could be of various nature for example in one of the latest cases, a change in personnel resulted in member of staff missing payment deadlines and nearly causing bad debt. Generator Member proposed reducing the time suppliers were given to make payments, however Supplier Member advised that in so doing it would increase the likelihood of Unsecured Bad Debt occurring.

Observer voiced the point that Generators must be paid on Thursday. It was asked that something be put in place to accommodate the required payments, K factors or licensing, etc. It was also stressed the need to look at what else can be achieved to deliver the code objectives. Also it was pointed out how important cash flow was and that all generators have to manage their cash flow and may be in a position of not knowing what they are going to get until late Thursday. Observer asked for SEMO/EirGrid to review how they could provide finance for limited shortfall events even by means of the parent company funding such shortfalls. MO Member dismissed this as a possibility, however all other potential options would be considered and the Panel was invited to submit views and further options to this regard.

Supplier Member asked what happens with the 95% of funds that are available and if it would be possible to assign them manually. MO Member advised that these would remain unused and that there was no capability to complete a manual calculation within the expected payment deadline and that the process must be system driven as much as possible to be fully accurate. Supplier asked if there was clear evidence early on in the process of what was the amount of bad debt at a macro level calculation. Proposal was voiced to make a calculation at the macro level and then make a payment based on that. MO Member advised there was no mechanism to do this.

Generator Member asked if there were to be more occurrences of this in the market then what are the penalties to defaulting participants. It was advised that Suppliers would receive default notices which could eventually see them out of the Market and also interest payments are issued. Generator Member asked if the process could be triggered on close of business Wednesday with credit draw downs on Thursday minus the shortfall. MO Member advised that the process cannot be stopped once it is started and therefore cannot be started until Unsecured Bad Debt is confirmed at 12:00 on Thursday, unless the time of remedy is shortened. This still means that the 95% of the money received could be paid on Friday with the remainder adjusted on the following week if the shortfall has been resolved.

Observer asked if MO could look at historic events to say what the implications would be for Generators. They also asked for an approximate range of the previous Unsecured Bad Debt amounts events that were narrowly missed. MO Member advised they had concerns with the disclosure of detailed data but that it would release as much possible within the confidentiality constraints. Observer suggested that the smearing be done earlier in the day in anticipation of bad debt to guarantee some payments. The issue is completing the calculation before the SRA’s. MO Member advised they would take on board the suggestions.

## Meeting **74 – 8 June 2017**

MO Member thanked the Committee for submitting comments in relation to this Modification per the action recorded at meeting 73. MO Member stated that summary responses to the comments received had been circulated prior to meeting 74.

MO Member indicated that the suggestion of finding ways to reduce the time taken to carry out the bad debt smearing process had been investigated and that it is not possible to complete the process, based on the current Trading and Settlement Code timelines, due to the time needed to process the calculations and ensure robust checking and approval. MO Member also advised that it is not possible to move the banking deadline for same day payments as this is a universal deadline set by the central banks.

Generator Member reiterated concerns in relation to revenue certainty and stated that the proposal tabled at meeting 73 to reset payment due timelines where Unsecured Bad Debt is invoked remains unacceptable. MO Member stated that SEMO were not pursuing this approach; however, were the proposed Modification not to be applied, SEMO would be in the position of having a Trading and Settlement Code obligation that it is not in a position to satisfy.

MO Member stated that SEMO understand the two main Participant concerns to be that Suppliers wish to maintain the time to remedy as 12:00 the day after the payment due date and that Generators wish to avoid any delay in being paid.

Generator Member stated that credit/collateral is held by SEMO to cover any shortfall and that this should be drawn on prior to initiating Unsecured Bad Debt. SEMO Member confirmed that credit/collateral is, and will continue to be, drawn down prior to initiating Unsecured Bad Debt and that by definition an Unsecured Bad Debt is a Shortfall which has not been remedied either through payment or posted Credit Cover.

MO Member advised that the alternative proposed by the Generator Member, to apply the smearing process prior to Unsecured Bad Debt being called in order to facilitate payment in line with the existing timelines, had been considered by SEMO. MO Member stated that they understood the appeal of this approach, in terms of preserving the time to remedy while still allowing for payment timelines to be maintained. MO Member stated that despite the benefits of this approach, it could result in SEMO smearing a Shortfall which was remedied prior to becoming an Unsecured Bad Debt. MO Member stated that this would be a fundamental change which would require further changes to the Trading and Settlement Code and that SEMO would not advocate an approach of reducing payments where Unsecured Bad Debt has not occurred.

MO Member went on to state that the intention of the proposal was not to change any underlying principle but to extend payment timelines by one day, in the event that Unsecured Bad Debt occurs, so that the payment obligation on SEMO is practically achievable. Generator Member stated that they wished to preserve the principle of being paid on the correct day.

Generator Member asked how many Shortfalls had occurred and how many of these had been remedied during the morning after the payment due date. MO Member stated that of five Shortfalls two were remedied the next morning. Generator Member stated that the Committee had requested SEMO to provide details of the historic amounts of Shortfalls and asked why this detail had not been provided. MO Member replied that SEMO have concerns over the disclosure of data on remedied defaults including as a percentage of total generator payments. MO Member also indicated that they felt that historic figures are not necessarily a good indication of likely future Shortfalls in any event, particularly given the small dataset.

Supplier Member asked why a point raised by the Committee in relation to treating the smearing of Unsecured Bad Debt and any subsequent Debit Note Excess as an iterative loop had not been addressed by SEMO in its summary responses. MO Member stated that although they were not certain that this was the intention of the Trading and Settlement Code drafting, SEMOs process results in a similar outcome and system changes are not an option in any event.

Generator Member asked MO Member how concerned they were about the prospect of not being able to meet the current Trading and Settlement Code obligations given the limited amount of time until the ISEM cutover date and the fact that the Unsecured Bad Debt smearing provision has not been called upon to date. MO Member asked the Generator Member how concerned they were about the prospect of payments being delayed by a day in the same context of the limited time until ISEM. MO Member went on to re-state that without the proposed change SEMO are in the position of having a Trading and Settlement Code obligation that they are not in a position to fulfil.

Supplier Member asked whether SEMO anticipated any similar issue for processing payment reductions resulting from Unsecured Bad Debt within the existing timelines for ISEM. MO Member stated that the Modification Proposal only applied to Part A of the Trading and Settlement Code and that system and process requirements for ISEM were based on the existing timelines. Supplier Member stated that they remained concerned about setting a precedent for ISEM.

Chairperson asked whether the Committee were happy to move to a vote on the proposed Modification. The Committee agreed to proceed to a vote.

At Meeting 74, the SEM Modifications committee took a vote on the Modification Proposal ‘Unsecured Bad Energy Debt and Unsecured Bad Capacity Debt timelines. The SEM Modifications committee, through a majority vote, that the Modification to be rejected.

# Proposed Legal Drafting

As set out in [Appendix 1](#_Appendix_1:_Mod_02_17)below.

#  LEGAL REVIEW

N/A

# IMPLEMENTATION TIMESCALE

N/A

# Appendix 1: Mod\_02\_17 v 1.0:

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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)* |
| **SEMO** | **24.01.2017** | **Urgent** | **Mod\_02\_17** |
| **Contact Details for Modification Proposal Originator** |
| **Name** | **Telephone number** | **Email address** |
| **Timothy Steele** |  | **Tim.steele@sem-o.com** |
| **Modification Proposal Title** |
| **Unsecured Bad Energy Debt and Unsecured Bad Capacity Debt timelines.** |
| **Documents affected***(delete as appropriate)* | **Section(s) Affected** | **Version number of T&SC or AP used in Drafting** |
| **T&SC****AP** | **T&SC –Section 6.50****AP15 3.4.1 (1.9)** | **V.18.0** |
| **Explanation of Proposed Change***(mandatory by originator)* |
| Under the current Trading and Settlement Code, a Defaulting Participant, wh applicable Debit Note to any pether for the full value or a shortfall on an Energy or Capacity Invoice amount, has up to 12:00 on the next Working Day after the Invoice Due Date to remedy the default. If the full Invoice or shortfall amount is not paid in full by this time, the amount shall become Unsecured Bad Debt.After this deadline the Market Operator shall, where practicable, withhold, deduct or set off payment of any amount due pursuant to the Code to the Defaulting Participant until the amount of the Unsecured Bad Debt and any applicable Default Interest has been recovered in full, begin the process of issuing Debit Notes to any Participant who is a SEM Creditor. In effect implementing the Bad Debt smearing process. In the event of Unsecured Bad Energy Debt and, or Unsecured Bad Capacity Debt, the Market Operator shall issue Debit Notes to the value of the Unsecured Bad Debt and pay each Self Billing Invoice less any applicable Debit Note to any Participant who is a SEM Creditor by paying the amount due from the SEM Trading Clearing Account and, or SEM Capacity Clearing Account as applicable to the SEM Creditors designated bank account or bank accounts for full value by the Self Billing Invoice Due Date. The Self Billing Invoice Due Date is 17:00, 4 Working Days after the date of the Self Billing Invoice. ( Section 6.50.5)The Market Operator is proposing an amendment to the Trading and Settlement Code timeline. In the event of Unsecured Bad Debt the new timelines detailed within T&SC Section 6.50.5 and Agreed Procedure 15 3.4.1 would allow for the following:* Issuing of Debit Notes to 17:00 5WD after the date of the Self Billing Invoice.
* Payment of the net Self Billing Invoices and Debit Notes by 17:00 5WD after the date of the Self Billing Invoice.

Alternative solutions have been considered and are summarised within the ‘Implications of not implementing the Modification Proposal’ section below. |
| **Legal Drafting Change***(Clearly show proposed code change using* ***tracked*** *changes, if proposer fails to identify changes, please indicate best estimate of potential changes)* |
| * 1. Payment shall be in accordance with the following:
1. each Ex-Post Indicative Settlement Statement, Initial Settlement Statement, Invoice and Self Billing Invoice shall be based on the data then available to the Market Operator at the time of its production;
2. each Invoice and Self Billing Invoice shall include the amount of all applicable charges and payments and shall include any applicable VAT charges;
3. each Debit Note (where applicable) shall include the amount of the Unsecured Bad Debt as set out in paragraph 6.56 and 6.57 as applicable and shall include any applicable VAT charges;
4. any invoiced Participant shall pay each Invoice in full without deduction, set-off or counterclaim (except as otherwise expressly provided for in the Code) by paying the amount due into the relevant SEM Trading Clearing Account or relevant SEM Capacity Clearing Account as applicable for full value by the Invoice Due Date; the Invoice Due Date is 12:00, 3 Working Days after the date of the Invoice; and
5. the Market Operator shall, subject to the provisions of the Code, pay each Self Billing Invoice, to any Participant who is a SEM Creditor by paying the amount due from the SEM Trading Clearing Account or SEM Capacity Clearing Account as applicable to the SEM Creditor’s designated bank account or bank accounts, for full value by the Self Billing Invoice Due Date which is 17:00, 4 Working Days after the date of the Self Billing Invoice.
6. the Market Operator shall, subject to the provisions of the Code, only in the event of Unsecured Bad Debt, pay each Self Billing Invoice less any applicable Debit Note to any Participant who is a SEM Creditor by paying the amount due from the SEM Trading Clearing Account or SEM Capacity Clearing Account as applicable to the SEM Creditor’s designated bank account or bank accounts for full value by Self Billing Invoice Due Date which is 17:00, 5 Working Days after the date of the Self Billing Invoice. The Market Operator shall implement Unsecured Bad Debt as per provisions set out in Paragraph 6.56 – 6.61

**Agreed Procedure 15 – Invoicing. Section 3.4.1**

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| I1.9 | Calculate and Issue Debit Note for Participants in respect of their Generator Units. | By 17:00 5 WD after the issue of the Self Billing Invoice in the event of Unsecured Bad Debt. |
| I1.10 | Pay the net of the Self Billing Invoice and the Debit Note to each Participant with a Self Billing Invoice. | By 17:00 5 WD after the issue of the Self Billing Invoice in the event of Unsecured Bad Debt. |

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| **Modification Proposal Justification***(Clearly state the reason for the Modification)* |
| The Market Operator has recently reviewed its internal processes including Unsecured Bad Debt. This review highlighted that under the current T&SC timelines ( Section 6.50 & Agreed Procedure 15) , System Functionality and external timelines, the Market Operator would be unable to complete the Bad Debt smearing process within the timelines set out in the Trading and Settlement Code and thereby in breach. The current timeline is to deliver the issuing of Debit Notes and net payment of Self Billing Invoices by 17:00 4 Working Days after the date of the Self Billing Invoice. Justification for this modification is due to the below points:* Bad Debt smearing, once implemented within the SEM Central Market System cannot be interrupted or cancelled.
* System Functionality – Under the current timelines, the functionality of the Central Market System, the Market Operator would be unable to deliver the Bad Debt smearing process given the current 14:30 cut off for Banking Payment Approvals.
* Potentially, all Settlement Runs relating to Energy and Capacity Markets may be processed as Unsecured Bad Debt due to Participant Defaults
* Large volume of Banking Payments requiring Senior Management Approval under current tight timeframes.
* Meticulous Internal checks and approvals.
* Complex process within the Market Operator.
* Potential disruption of Participants internal processes under stressed timeframes.

Given the financial implications and the processing of Unsecured Bad Debt under tight timelines, the Market Operator feels that this Modification if passed would release the pressures of implementing this protracted process whereby the all necessary diligence, approvals and banking cut off timelines could be met. If passed, this modification would be implemented within the current T&SC for the current SEM market. The Market Operator will review the Technical specifications and requirements regarding Unsecured Bad Debt within the I-SEM Market. |
| **Code Objectives Furthered***(State the Code Objectives the Proposal furthers, see Section 1.3 of T&SC for Code Objectives)* |
| Section 1.3:2. to facilitate the efficient, economic and coordinated operation, administration and development of the Single Electricity Market in a financially secure manner |
| **Implication of not implementing the Modification Proposal***(State the possible outcomes should the Modification Proposal not be implemented)* |
| Under the current timelines and the financial implications, the Market Operator has explored alternative options regarding this modification, though we feel that the recommendation detailed above would provide an efficient end to end process of the Bad Debt smearing process, a direct result of implementing Unsecured Bad Debt within the SEM.Alternative options are: 1. Adjust the current timelines of time to remedy of the default from 12:00 next working day after the Invoice Due Date **to** 17:00 same Working Day of the Invoice Due Date
2. Adjust the current timelines of time to remedy of the default from 12:00 next working day after the Invoice Due Date **to** 07:00 next working day after the Invoice Due Date.

The Market Operator believes that the above alternative options would carry an unnecessary risk for Market Participants operating within the current SEM as this may increase the chances of Unsecured Bad Debt along with decreasing the time in which is given to a defaulting participant to remedy the full Invoice or shortfall amount. The irreversibility of the Bad Debt smearing process within the Central Market Systems and the strict deadlines for banking payments approvals would still remain and carry an unnecessary business risk to both the Market Operator and Market Participants. |
| **Working Group***(State if Working Group considered necessary to develop proposal)* | **Impacts***(Indicate the impacts on systems, resources, processes and/or procedures)* |
| No | System Impacts:* There are no system impacts as a result of the Modification.

Resource Impacts:* There are no resource impacts as a result of the Modification on the Market Operator, though there may be potential resourcing impacts on Participants.

SEM Impacts* Participant’s financial position to be accessed on an Individual basis.
* SEM Creditors, payment of Self Billing Invoices less Debit Note would be by 17:00 5WD after the date of the Invoice.
* Reduce potential instances in where by Unsecured Bad Debt may be implemented.

 All processes and procedures Unsecured Bad Debt as detailed above  |
| ***Please return this form to Secretariat by email to*** ***modifications@sem-o.com*** |