

Title: Ofgem Monitoring Powers for Nominated Electricity Market Operators IA No: DECC0216 RPC Reference No: RPC-3327(1)-DECC Lead department or agency: Department of Energy and Climate Change Other departments or agencies: Ofgem	Impact Assessment (IA)			
	Date: 27/04/2016			
	Stage: Final			
	Source of intervention: EU			
	Type of measure: Secondary legislation			
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Summary: Intervention and Options				RPC Opinion: GREEN

Cost of Preferred (or more likely) Option				
Total Net Present Value	Business Net Present Value	Net cost to business per year (EANDCB in 2014 prices)	One-In, Three-Out	Business Impact Target Status
£m	£m	£m	Not in scope	N/A

What is the problem under consideration? Why is government intervention necessary?

The UK is currently implementing EU regulations establishing guidelines on capacity allocation and congestion management (CACM regulation). The CACM Regulation promotes the sharing of liquidity across the European market and clearer investment signals for the placement of generation and interconnector assets. This generates benefits to consumers through improvements in the efficiency of the electricity market and security of supply. The CACM regulation requires power exchanges designated as Nominated Electricity Market Operators (NEMOs) to cooperate internally and across borders to deliver market coupling operations. The CACM regulation requires designating authorities (Ofgem in the case of GB) to monitor all NEMOs performing single day ahead and/or intraday coupling within their member state, and ensure compliance by all NEMOs with the requirements of the CACM regulation. Ahead of market coupling BEIS considers it necessary to implement changes to UK legislation to avoid the risk of potentially unreliable and inefficient access to cross-border trading because of insufficient enforcement powers. To fully implement the above requirements an appropriate regulatory framework for NEMOs in GB needs to be established.

What are the policy objectives and the intended effects?

The policy aims to ensure that NEMOs, which will operate an exclusive route to short term cross-border trading, are regulated to deliver reliable, robust, and cost-efficient market coupling. Unreliable and inefficient access to cross-border trading for market participants may disrupt or distort the wider wholesale market with detrimental impacts on consumers.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

BEIS has conducted a targeted consultation with directly affected parties on the proposals to give Ofgem powers to monitor NEMOs to ensure CACM requirements are implemented correctly. Following review of the consultation responses, this impact assessment considers two different ways in which the regulation of NEMOs can be implemented, a do nothing and a preferred option:

Do nothing - Ofgem would undertake general monitoring through public information, rely on voluntary information from NEMOs, and use limited powers to request information from NEMOs through the CACM regulation. The only enforcement power available to Ofgem would be to revoke designation for non-compliant NEMOs, a procedure set out in the CACM regulation.

Make NEMOs Regulated Persons in the Electricity Act (preferred option): The definition of Regulated Person in the Electricity Act 1989 (the "Electricity Act") would be amended to include NEMOs and the requirements of CACM, relevant to NEMOs, would be added to schedule 6A. Such requirements would become enforceable using the existing enforcement regime set out in sections 25 to 28 (inclusive) of the Electricity Act.

BEIS considered alternative options and tested stakeholders views on them. All of these were considered to be less well fitted to the policy objectives and likely to impose disproportionate burdens on affected businesses.

Will the policy be reviewed? It will/will not be reviewed. If applicable, set review date: Month/Year					
Does implementation go beyond minimum EU requirements?			No		
Are any of these organisations in scope?		Micro No	Small No	Medium No	Large No
What is the CO ₂ equivalent change in greenhouse gas emissions? (Million tonnes CO ₂ equivalent)			Traded:		Non-traded:

I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) that the benefits justify the costs.

Signed by the responsible Minister:

Neville-Rolfe

Dat

e:

22-Oct-2016

Summary: Analysis & Evidence

Policy Option 0

Description: Do nothing - Ofgem would undertake general monitoring through public information, rely on voluntary information from NEMOs, and use limited powers to request information from NEMOs through the CACM regulation. The only enforcement power available to Ofgem would be revocation of designation for non-compliant NEMOs, a procedure set out in the CACM regulation.

FULL ECONOMIC ASSESSMENT

Price Base Year	PV Base Year	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	High: Optional	Best Estimate:

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	Optional	Optional	Optional
High	Optional	Optional	Optional
Best Estimate			

Description and scale of key monetised costs by 'main affected groups'

There is no change to legislation under Policy Option 0 ('Do Nothing') and therefore there are no additional costs. This option is set out here as it serves as the baseline against which Option 1 is assessed. Costs could not be quantified.

Other key non-monetised costs by 'main affected groups'

There are baseline costs for Ofgem and NEMOs. Ofgem faces costs associated with the monitoring process of NEMOs. Ofgem expects these costs to be subsumed in business as usual costs. NEMOs would face costs with regards to complying with information requested by Ofgem. However, consultation responses suggest that costs of complying with Ofgem monitoring process would be negligible. This option is unlikely to provide Ofgem with sufficient powers to ensure compliance is enforced and fully monitored, and, as a consequence, deter NEMOs from non-compliance. Potential second order costs for society for Option 0, linked to the risks of a weaker legal basis within which Ofgem can monitor NEMOs, are set out in the risks section below.

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	Optional	Optional	Optional
High	Optional	Optional	Optional
Best Estimate			

Description and scale of key monetised benefits by 'main affected groups'

There is no change to legislation under Policy Option 0 ('Do Nothing') and therefore there are no additional benefits. This option is set out here as it serves as the baseline against which Option 1 is assessed. Benefits could not be quantified.

Other key non-monetised benefits by 'main affected groups'

Assuming compliance with CACM requirements by NEMOs, even in the case of Ofgem not having a sound legal basis to monitor NEMOs and enforce compliance, the proposals would benefit market participants as NEMOs would effectively enable market coupling and this would improve efficiency in the market. As a consequence this would translate in better outcomes for consumers. The wider benefits should be the same as those identified under Option 1 (see following page). However under this option NEMOs would face weaker deterrence for non-compliance and therefore the option would bear higher risks than Option 1, as outlined in the risk section. Therefore we consider that this option does not provide sufficient incentives for NEMOs to comply with regulation and achieve the policy intended benefits.

Key assumptions/sensitivities/risks	Discount rate (%)	
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Ofgem does not think they can rely directly on the CACM regulation or any existing powers to request information or ensure compliance with respect to monitoring or ensuring compliance with NEMO obligations, as the provisions stated in CACM regulation are not sufficiently precise and do not provide, in itself, an adequate regulatory framework. Non-compliance with the NEMO designation criteria and relevant tasks poses significant risk to the efficient and competitive operation of the GB wholesale market. Unreliable and inefficient exclusive access to cross-border trading in the day ahead and intraday timeframes via NEMOs may distort the wider wholesale market and prevent achievement of efficiencies which would put downward pressures on wholesale prices, with detrimental impact on consumer bills. As such this option would not provide full range of regulatory tools and would limit Ofgem's ability to provide a credible deterrence against non-compliance or a visible and meaningful consequence for businesses who fail consumers.

Additional costs to NEMOs to comply with Ofgem monitoring requests will depend on the process that Ofgem will establish for continued monitoring. Under Option 0 NEMOs would only comply with Ofgem's requests on a voluntary basis and Ofgem could only rely on revocation as deterrence mechanism.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			Score for Business Impact Target (qualifying provisions only) £m:
Costs:	Benefits:	Net:	
			Less than £1m (negligible impact)

Summary: Analysis & Evidence

Policy Option 1

Description: Make NEMOs Regulated Persons in the Electricity Act (preferred option): The definition of Regulated Person in the Electricity Act 1989 (the “Electricity Act”) would be amended to include NEMOs and the requirements of CACM, relevant to NEMOs, would be added to schedule 6A. Such requirements would become enforceable using the existing enforcement regime set out in sections 25 to 28 (inclusive) of the Electricity Act.

FULL ECONOMIC ASSESSMENT

Price Base Year	PV Base Year	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	High: Optional	Best Estimate:

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	Optional	Optional	Optional
High	Optional	Optional	Optional
Best Estimate			

Description and scale of key monetised costs by ‘main affected groups’

Consultation responses did not provide quantitative estimates of additional costs from this option, but the vast majority of responses suggest additional costs are expected to be minimal.

Other key non-monetised costs by ‘main affected groups’

If any, additional costs from this option compared to Option 0 are likely to apply to Ofgem and NEMOs. NEMOs would face some costs of compliance in terms of providing regular material to prove compliance and/or respond to requests from Ofgem to demonstrate compliance. Consultation responses suggest that this cost is likely to be minimal, if not negligible. Ofgem suggested its costs associated with their requests for information would be the same under both options and that the costs associated with the monitoring process of NEMOs would be subsumed in business as usual costs. Therefore, Option 1 would not have any or very minimal additional costs compared to Option 0. The proposed legislative change, i.e. amending the Electricity Act, is assumed to provide minimal regulatory burden. Consultation responses agreed with this assessment.

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	Optional	Optional	Optional
High	Optional	Optional	Optional
Best Estimate			

Description and scale of key monetised benefits by ‘main affected groups’

Consultation responses did not provide quantitative estimates of benefits from this option.

Other key non-monetised benefits by ‘main affected groups’

Under Option 1 Ofgem has a sound legal basis to monitor NEMOs and enforce compliance. This implies that the proposals would benefit market participants as NEMOs would have stronger incentives to effectively enable market coupling that would improve efficiency in the market. As a consequence this would avoid the risks outlined under Option 0 and translate in better outcomes for consumers. Consultation respondents identified several wider benefits from effective monitoring of NEMOs, including: Contribution to a level playing field for multiple NEMOs operating in a bidding zone; Ensuring that NEMOs carry out their responsibilities in a timely manner; Ensuring that market coupling processes remain efficient, and potentially promote initiatives to improve efficiency further; Improved confidence for market participants taking part in trading arrangements thanks to the parties involved being subject to the appropriate level of regulatory oversight.; Ensuring flexible, effective, and cost-efficient monitoring of NEMOs activities in GB; Benefits to consumers and market participants from creating a robust, transparent and efficient supervision regime of market coupling activities. Given the stronger legal basis within which Ofgem would be able to monitor NEMOs under Option 1 compared to Option 0, we consider that the probability of achieving the identified market benefits is higher under this option compared to Option 0.

Key assumptions/sensitivities/risks	Discount rate (%)
Additional costs to NEMOs to comply with Ofgem monitoring requests depend on the process that Ofgem will establish for continued monitoring. Under Option 1 Ofgem could rely on a sound legal basis to enforce compliance.	

BUSINESS ASSESSMENT (Option 2)

Direct impact on business (Equivalent Annual) £m:			Score for Business Impact Target (qualifying provisions only) £m:
Costs:	Benefits:	Net:	
			Less than £1m (negligible impact)

Evidence Base (for summary sheets)

Problem under consideration

1. The UK is currently implementing a number of regulations approved under the European Union's Third Package of legislation on the internal energy market, which came into force in 2009. The Third Package provides for a number of technical regulations related to cross-border trade to be adopted by the Commission and Member States. One of these regulations establishes guidelines on capacity allocation and congestion management (CACM Regulation) in order to put in place harmonised trading arrangements across interconnectors known as "market coupling". This is a congestion management method where interconnection capacity and electricity is sold at the same time in one daily day-ahead auction and then continuously during the intra-day period. The CACM Regulation therefore promotes the sharing of liquidity across the European market and clearer investment signals for the placement of generation and interconnector assets. This generates benefits to consumers through improvements in the efficiency of the electricity market and security of supply.
2. Market coupling rules have already been implemented on the interconnectors connecting GB to France and Netherlands in 2014¹. However, in addition to the rules on market coupling that the UK is already applying, the CACM Regulation introduces a number of procedures which are essential for proper functioning of market coupling.
3. Under one of these procedures the CACM regulation requires power exchanges designated as Nominated Electricity Market Operators (NEMOs) to cooperate internally and across borders to deliver market coupling operations. Prospective NEMOs apply for designation to National Regulating Authorities (NRAs) (Ofgem in the case of GB) and are designated as such if they meet the required criteria.
4. The CACM regulation requires designating authorities (Ofgem in the case of GB) to monitor all NEMOs performing single day ahead and/or intraday coupling within their member state, and ensure compliance by all NEMOs with the requirements of the CACM regulation. Therefore, BEIS considers that changes are needed to UK legislation to establish an appropriate regulatory framework of NEMOs in GB.
5. BEIS has conducted a targeted consultation with directly affected parties on the proposals to give Ofgem powers to monitor NEMOs and ensure CACM requirements are implemented by NEMOs. Following review of the consultation responses, this impact assessment considers two different ways in which the regulation of NEMOs can be implemented; a do nothing and a (preferred) policy option.

Rationale for intervention

6. NEMOs are responsible for the on-going operation of a number of market coupling functions. These include developing, maintaining and operating the algorithms, systems and procedures needed for the day-ahead and intra-day market and validating and disseminating the results of trading.
7. Ofgem, as NRA for GB, is required to monitor the on-going compliance with designation criteria of each NEMO designated in GB and to ensure compliance with the CACM regulation by all NEMOs performing single day-ahead and/or intra-day coupling within GB².
8. BEIS believes changes to legislation are required, to ensure that Ofgem has sufficient powers to meet its obligations. Where necessary, Ofgem must have appropriate powers to gather information required to satisfy itself of NEMOs on-going compliance with CACM, to investigate further where non-compliance is suspected, and to take necessary enforcement action to secure compliance. The expectation is that NEMOs will fully comply with the requirements of CACM and respond to Ofgem's informal requests for information. However, a credible deterrence against non-compliance and a visible and meaningful consequence for businesses who fail consumers is required both to ensure compliance and to provide wider market participants with confidence that these functions are appropriately regulated.

¹ Market coupling has been implemented in the day-ahead timeframe only.

² In accordance with Article 19 of Regulation (EC) No 714/2009. In addition to providing day-ahead and intra-day trading in the Member State in which they are designated, NEMOs have the right offer these services in other Member States, subject to certain exceptions

9. Effective regulation of NEMOs, which will conduct important functions that benefit the wider market, ultimately contributes to Ofgem achieving its objectives of better outcomes for consumers and better functioning markets for companies within the sector. Not providing Ofgem with the necessary powers to ensure NEMOs comply with CACM regulation would make the UK non-compliant with CACM requirements, and might undermine the objectives of CACM to achieve a harmonised system where market coupling is implemented effectively across Member States.

Policy objective

10. The policy aims to ensure that NEMOs, which will operate an exclusive route to short term cross-border trading, are regulated to deliver reliable, robust, and cost-efficient market coupling. Unreliable and inefficient access to cross-border trading for market participants may disrupt or distort the wider wholesale market with detrimental impacts on consumers.

Description of options considered (including do nothing)

11. Following a targeted consultation with directly affected parties, we are presenting two options for the implementation of the Regulation of Nominated Electricity Market Operators (NEMOs).

0. Do nothing
1. Make NEMOs Regulated Persons in the Electricity Act (preferred option)

12. Each option considers a different way in which Ofgem would meet its obligations to monitor and enforce NEMO activities. The options are explained in more details in this section.

Do nothing

13. Under this option, Ofgem would undertake general monitoring through public information, rely on voluntary information from the NEMOs, and use limited powers to request information from NEMOs through the CACM regulation. CACM sets out procedures for revoking the designation of non-compliant NEMOs. This would be the only enforcement power available to Ofgem. Therefore, the possibility of the designation being revoked, in the event of non-compliance with designation criteria, would be used to ensure compliance.

Make NEMOs Regulated Persons in the Electricity Act

14. Under this option, the definition of Regulated Person in the Electricity Act, which includes individuals and organisations whose relevant activities are regulated by the Authority and subject to the monitoring and enforcement powers set out in the Act, would be amended to include NEMOs. In addition the requirements of CACM, relevant to NEMOs, would be added to Schedule 6A³. Such requirements would become enforceable using the existing enforcement regime set out in sections 25 to 28 (inclusive) of the Electricity Act.
15. There would be further obligations on NEMOs to cooperate with Ofgem to enable it to monitor NEMO activities:
- NEMOs must report in a timely manner to the Authority in case it identifies any instance of or potential for non-compliance with criteria, tasks, and objectives of the CACM regulation,
 - NEMOs must provide information in relation to the criteria, tasks, and objectives of the CACM regulation that may be requested by the Authority.
16. It is important to note that there is no difference between Option 0 and Option 1 in terms of monitoring activities and requests that Ofgem's would make to NEMOs as Ofgem would need to monitor NEMOs and NEMOs would need to make sure they are compliant with the CACM

³ Schedule 6A: Inserted by The Electricity and Gas (Internal Markets) Regulations 2011: www.legislation.gov.uk/ukSI/2011/2704/schedule/4/made

regulations under both of these two options. The only difference is that Option 1 would give Ofgem a stronger legal basis within which to supervise NEMOs and it requires legislative change, whereas under Option 0 Ofgem would rely on NEMOs responding to its requests on a voluntary basis.

Alternative options

17. BEIS considered alternative options and tested stakeholders views on them during the consultation. Other options considered include regulating NEMOs through wider regulation of power exchanges or creating a new license for NEMOs; or regulating them through an existing licensee. BEIS however felt these options to be less well fitted to the policy objectives, and in particular would be likely to impose disproportionate burdens on affected businesses. Consultation responses confirmed this view, and these options have therefore been discarded and are not presented in the final IA.

Monetised and non-monetised costs and benefits of each option (including administrative burden)

Option 0: Do nothing

BENEFITS:

18. This option would not require changes to existing regulatory framework and Ofgem's only enforcement route would be to revoke NEMO's designation or the threat of potential revocation to encourage compliance with CACM requirements. Ofgem would rely on NEMOs responding to its information requests on a voluntary basis.
19. While this option could contribute to the achievement of the CACM regulation objectives of maximising the efficient use of interconnection and ensuring that flows follow prices, therefore improve market conditions⁴, this option is unlikely to provide Ofgem with sufficient powers to ensure compliance is enforced and fully monitored, and, as a consequence, deter NEMOs from non-compliance. As explained in the risk section, it is considered that Option 0 would bring limited contribution to the achievement of the policy objective of effective and ongoing implementation of CACM requirements as the only tool available to Ofgem against non-compliance would be to revoke designation, largely considered a last-resort. . NEMOs would have no legal requirement to respond to Ofgem's request to provide information about their activities, leading to a higher risk of infringement going undetected. The risk section further explores the risks and second order costs of this Option.

COSTS:

20. There are two parties that could face **direct costs** from this option, NEMOs and Ofgem.

NEMOs

21. NEMOs might face compliance costs in terms of providing regular material to prove on-going compliance and/or respond to requests from Ofgem to demonstrate compliance. However this would be done on a voluntary basis or in response to requests from the EU Agency for the Cooperation of Energy regulators (ACER).
22. Consultation responses did not provide any estimate of cost of compliance but suggested that, under Option 1, these would be very small if not negligible. Based on this we have no evidence on which we can quantify these costs. Given that Ofgem's monitoring approach would be the same under both options, we would expect costs under Option 0 to be the same as Option 1.

⁴ Effective achievement of market coupling is expected to improve security of supply, and increase competition and market integration, which would lead to cost efficiencies.

23. Albeit small, costs of compliance could be passed through to market participants who operate on exchanges, for example via an increase in membership fees. These costs could then be passed on to consumers. In reference to Option 1, consultation responses suggest that additional costs from the proposals are unlikely to be material, and we would expect this to be the same under Option 0.

Ofgem

24. Ofgem expects to be able to conduct monitoring activities on NEMOs as part of its ongoing monitoring processes. Resource costs specific to the monitoring of NEMOs are expected to be subsumed in business as usual costs. Potential second order costs for society for Option 0, linked to the risks of a weaker legal basis within which Ofgem can monitor NEMOs, are set out in the risks section below.

RISKS:

25. It is the opinion of Ofgem that they cannot directly rely on the CACM regulation or any existing powers to request information or ensure compliance with respect to monitoring or ensuring compliance with NEMO obligations. CACM Regulation states that NRAs are required to monitor and ensure compliance, however the provision is not sufficiently precise and does not provide, in itself, an adequate regulatory framework, leaving significant aspects of NEMO requirements outside the scope of Ofgem's regulatory powers. It is therefore possible that the European Commission could find UK implementation deficient, and start infringement proceedings if steps were not taken to provide Ofgem with appropriate powers.

26. Non-compliance with the NEMO designation criteria and relevant tasks poses significant risk to the efficient and competitive operation of the GB wholesale market. Unreliable and inefficient exclusive access to cross-border trading in the day ahead and intraday timeframes via NEMOs may disrupt and distort the wider wholesale market with detrimental impact on consumer bills. As such this option would not provide full range of regulatory tools and would limit Ofgem's ability to provide a credible deterrence against non-compliance or a visible and meaningful consequence for businesses who fail consumers. If this risk was to materialise there would be **indirect (second order) costs** for other compliant NEMOs as their ability to achieve market coupling might be compromised, other market participants and eventually consumers who would not fully benefit from the efficiencies enabled by market coupling.

27. In addition, while Ofgem's powers under alternative enforcement areas, e.g. REMIT⁵ and Competition⁶, do allow Ofgem to monitor and take appropriate action with respect to market abuse (disclosure of inside information, reporting of suspicious activity, and anti-competitive behaviour, and some NEMO activities may fall within these categories), these powers do not cover NEMOs' obligations and in particular their requirement to comply with the designation criteria or deliver single day ahead and/or intraday coupling.

28. While this option would not require legislative change, Ofgem does not think it provides a sufficient regulatory framework, leaving significant aspects of NEMO requirements outside the scope of its regulatory powers. It would not meet Ofgem's strategic outputs for consumer outcomes or principles for better regulation.

Option 1: Make NEMOs Regulated Persons in the Electricity Act (preferred option)

BENEFITS:

29. This option would provide Ofgem with powers to request information and take enforcement action for all NEMO obligations. It would also provide flexibility to monitor and ensure compliance in line with

⁵ The EU REMIT regulation [<http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32011R1227&from=EN>], which has been in force since 28 December 2011, prohibits insider trading and market manipulation in wholesale energy markets across the EU

⁶ Ofgem's principal objective is to protect the interests of existing and future electricity and gas consumers, which Ofgem does in a number of ways, including the supervision and development of markets and competition (<https://www.ofgem.gov.uk/about-us/who-we-are>). Ofgem is governed by the Gas and Electricity Markets Authority, whose powers and duties are laid out in legislation (<https://www.ofgem.gov.uk/publications-and-updates/powers-and-duties-gema>)

existing powers and its commitments to better regulation. This provides a regulatory framework for Ofgem that acts as a credible deterrence against non-compliance providing confidence to the market that the operation of market coupling is efficient and robust.

30. It provides appropriate powers for Ofgem to use information requests and enforcement powers in line with its commitments to better regulation. It does not go beyond the requirements of EU law. Therefore, from Ofgem's perspective, this should provide appropriate regulatory oversight of NEMOs, and ensure that GB is fully compliant with EU law.
31. Consultation responses suggested that stakeholders believe this option to be the most suitable to fulfil the regulation requirements. Respondents agreed that Ofgem should have the necessary enforcement powers to ensure NEMOs are compliant with CACM regulation, and ensure robust and cost-efficient market coupling can be achieved. The approach proposed under this option was seen as proportionate, as it would impose a minimal regulatory burden while ensuring Ofgem has the necessary resources needed to monitor NEMOs operating in its bidding zone.
32. Consultation respondents did not provide quantitative estimates of benefits for this proposal, but identified several benefits from a qualitative perspective:
- Contribution to a level playing field for multiple NEMOs operating in a bidding zone; market participants would benefit from Ofgem ensuring that all joint NEMOs tasks are performed, so that all matched orders are carried out;
 - Ensuring that NEMOs carry out their responsibilities in a timely manner;
 - Ensuring that market coupling processes remain efficient, and potentially promote initiatives to improve efficiency further;
 - Improved confidence for market participants taking part in trading arrangements thanks to the parties involved being subject to the appropriate level of regulatory oversight;
 - Ensuring flexible, effective, and cost-efficient monitoring of NEMOs activities in GB;
 - Benefits to NEMOs from establishing a level playing field in a cost-efficient manner;
 - Benefits to consumers and market participants from creating a robust, transparent and efficient supervision regime of market coupling activities.
33. Given the stronger legal basis within which Ofgem would be able to monitor NEMOs under Option 1 compared to Option 0, we consider that the probability of achieving the identified market benefits is higher under this option compared to Option 0.

COSTS:

34. There are two parties that could face **direct costs** from this option, NEMOs, and Ofgem.

NEMOs

35. NEMOs would face some costs of compliance in terms of providing regular material and/or responding to requests from Ofgem to demonstrate compliance. Consultation responses suggest that this cost is likely to be minimal, if not negligible. One respondent suggested that data on market coupling is either already available or soon will be, as providers are required to provide these data to NRAs, hence the additional costs of this proposal are unlikely to be significant. This view was shared by a range of market participants and NEMOs themselves. One party pointed out how costs will depend on the process that Ofgem establishes for continued monitoring, and argued for these costs to be kept at a minimum. However, respondents were unable to provide exact estimates of costs.
36. Costs of compliance could be passed through to market participants who operate on exchanges, for example via an increase in membership fees. These costs could then be passed on to consumers. Consultation responses did not provide an estimate of either the additional cost of compliance and how this would be passed through to market participants, however, based on evidence received we expect the impact to be small. Some respondents did point out that, should costs to NEMOs increase as a consequence of this proposal, only reasonable efficient and proportionate costs should be

recovered by NEMOs' fees. If this occurred they would be passed on to market participants and eventually consumers.

Ofgem

- 37. As per Option 0, Ofgem expects to be able to conduct monitoring activities on NEMOs as part of its ongoing monitoring processes. Resource costs specific to the monitoring of NEMOs are expected to be subsumed in business as usual costs. In the event of non-compliance, there would be second order (indirect) costs to society, as the market would not achieve the efficiencies associated with market coupling, and this could have detrimental impacts on consumer bills.
- 38. Overall it is important to note that this option is not expected to create more on-going costs than Option 0, as under both options Ofgem will need to monitor and make requests to NEMOs. The only difference is that under Option 1 Ofgem has firmer legal framework to do so.

Rationale and evidence that justify the level of analysis used in the IA (proportionality approach)

- 39. Requirements to provide Ofgem with appropriate enforcement powers to allow it to conduct its monitoring activity on NEMOs follow directly from CACM regulations. Currently, only two parties in GB will have to comply with the requirements: the two power exchanges that have been designated as NEMOs by Ofgem. BEIS therefore considered it appropriate to hold a targeted consultation with directly affected parties rather than a wider formal consultation.
- 40. The consultees have not raised major concerns about the proposals, and in fact agree that the preferred option proposed by BEIS is the most suitable to balance fulfilment of CACM requirements from a regulatory perspective while having the minimum impact in terms of increased regulatory burden compared to alternative options. Therefore, BEIS considered it appropriate to base costs and benefits on views provided by consultation responses, without conducting wider and more complex analysis.

Risks and Assumptions

- 41. Estimates of cost and benefits are based on responses from consultees. Once the monitoring processes are in place, it is possible that these estimates might result in over- or under-estimates. In particular, should costs have been underestimated, this might result in higher costs to market participants operating on exchanges, which might be passed through to consumers. BEIS considers this risk to be low as it is one of the Government objectives to keep the impact of regulatory burden on businesses low. This is reflected in the operational approach of regulatory bodies, including Ofgem.

Direct costs and benefits to business calculations (following OITO methodology)

42. The following table summarises the Options and whether they are in or out of scope of OITO.

Table: In or Out of Scope Options

	Option	In or out of scope of OITO
1	Do nothing	OUT
2	Make NEMOs Regulated Persons in the Electricity Act	OUT

- 43. The OFGEM monitoring powers for NEMOs form part of EU regulation (Regulation (EU) 2015/1222) on CACM and so fall out of scope of OITO as a Non-Qualifying Regulatory Provision. In addition, the preferred option has no direct costs to business and so has an EANCB equal to 0. The proposed approach represents the minimum required for Ofgem to meet its obligations under the EU

legislation.

Rationale for Fast Track status:

44. The gross costs to business of this policy do not exceed £1m in any given year therefore the policy qualifies for the Fast Track. The cost of the implementation of this EU Regulation to business will be £0.
45. The department has submitted a low cost NQRP form to the RPC and they have validated the EADCB of 0 as well as this IAs NQRP status.

Wider impacts

46. The main wider impact identified is possible improved confidence in the market for parties operating in the market. Besides NEMOs, all other parties operating in the UK market, such as suppliers, generators, TSOs, DSOs, and interconnectors, would be assured that market coupling is implemented under Ofgem supervision. Also, parties operating in other Member states would benefit from confidence that Ofgem is properly carrying out its monitoring tasks on the UK side. This might provide a further incentive to cross border trading and generate better outcomes for the UK market such as higher liquidity in the wholesale market, which might drive down prices, as well as providing further market routes that could further support the UK security of supply. Increased confidence by market participants might result in more stable market and therefore increase consumer confidence in the market.

Summary and preferred option, with description of implementation plan.

47. BEIS's preferred option is to amend the Electricity Act 1989 so that existing enforcement powers (contained in Sections 25-28) can be applied to NEMOs. This would be achieved by including NEMOs within the definition of Regulated Person and adding the NEMO requirements of CACM to a new category of relevant requirements within Schedule 6A. These amendments would be made by regulations under section 2(2) of the European Communities Act 1972.
48. It is anticipated that NEMOs will be engaged in implementation activities, ahead of market coupling, from autumn 2016. These activities are critical to implementation of CACM, so it is desirable that Ofgem have appropriate enforcement powers by the autumn.