



**Discussion Paper on ‘The impact of Brexit on the Single Electricity Market (SEM) and the Future of the Internal Energy Market (IEM)’**

## Introduction:

On 27 March 2019, the British Irish Chamber of Commerce (the Chamber) and Energy UK held a Roundtable Dialogue on 'The Impact of Brexit on the Single Electricity Market (SEM) and the Future of the Internal Energy Market (IEM)', hosted by Eversheds Sutherland, Dublin. This was the second collaboration between the Chamber and Energy UK following on from the Policy Forum 'The Future of the UK – Ireland Energy Relationship', held in London in February 2019.<sup>1</sup>

This paper will set out the context in which the Roundtable was held, the objectives of the discussion and the main points raised by participants. This Paper will be distributed to key stakeholders including businesses, regulators, representative associations and the relevant government departments in Ireland, Northern Ireland, Great Britain and the EU.

## Summary of Key Points:

- **Protection of the Single Electricity Market (SEM)** on the island of Ireland is the collective responsibility of all stakeholders. The Withdrawal Agreement and Political Declaration on the Future Relationship between the EU and UK establishes a framework in which this can be achieved.
- While divergence on 'Day 1' post-Brexit will not happen, **subsequent divergence** would make the efficient operation of the SEM difficult. However, the SEM local market and the SEM Great Britain intraday auctions should and can be maintained even allowing for the impacts of Brexit.
- **The UK remaining fully aligned to the IEM** is in the best interests of Ireland, the UK and the EU.
- The UK should continue its **participation in the EU Emissions Trading System (EU ETS)**, or alternatively the domestic UK ETS should be linked to the EU ETS.
- Where possible, the UK should continue its **participation in EU bodies and agencies** such as Eurelectric and Eurogas.
- In the UK's absence from the Council of Ministers, Commission and Parliament there is an onus on the UK and Irish governments to **increase bilateral engagement** in this area.

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<sup>1</sup> The Report of that meeting is available at <https://www.britishirishchamber.com/wp-content/uploads/2017/04/Energy-Brochure-Web-Version-2.pdf>

## Setting the Context of the Meeting:

### 1) The Single Electricity Market (SEM) on the Island of Ireland

Since 2007, the island of Ireland has operated as a Single Electricity Market (SEM), which provides the least cost source of electricity to the benefit of all consumers on the island of Ireland. It currently operates within the framework of common EU rules on electricity markets. It has benefited all stakeholders especially consumers who have benefitted from the economies of scale.

While the final date of the UK's exit from the EU is in flux, from the viewpoint of Energy stakeholders there are two distinct scenarios for consideration:

1. **Scenario 1:** The Withdrawal Agreement between the UK and the EU is ratified (transition/implementation period concludes 31 December 2020),
2. **Scenario 2:** A 'No Deal' outcome, under this scenario the United Kingdom would leave the European Union without a Withdrawal Agreement.

**Scenario 1:** The EU and the UK reached an agreement on the Single Electricity Market as part of the Ireland/Northern Ireland Protocol of the Withdrawal Agreement. Should the Withdrawal Agreement be ratified by the EU and the UK, the current operations of the SEM will remain in place until superseded by new arrangements. In addition, the Political Declaration sets out an ambition for close collaboration that can support a framework for the maintenance of the SEM:

*“The Parties should establish a framework to facilitate technical cooperation between electricity and gas networks operators and organisations, such as the European Networks of Transmission System Operators for Electricity and Gas, in the planning and use of energy infrastructure connecting their systems. The framework should also include mechanisms to ensure as far as possible security of supply and efficient trade over interconnectors over different timeframes”.*<sup>2</sup>

**Scenario 2:** While protecting the SEM has been outlined as a priority for both the UK and Irish Governments, concerns have intensified over the feasibility of the initiative in a 'No Deal' scenario or in the case of regulatory divergence between the UK and the Internal Energy Market (IEM) post-Brexit. To minimise the disruption to the SEM in a 'No Deal' scenario, both governments have taken legislative action.

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<sup>2</sup> (Article XI, Political Declaration setting out the Framework for the Future Relationship between the European Union and the United Kingdom)

**The Irish Government's Response:** 'Withdrawal of the United Kingdom from the European Union (Consequential Provisions) Bill 2019'<sup>3</sup>.

As part of the Irish Government's 'Omnibus Bill', in order to ensure there are no issues of non-compliance of EU law, the Government amended the 'Electricity Regulation Act 1999' to allow the Commission for Regulation of Utilities (CRU) to quickly modify licences of Irish-based participants in SEM on a temporary basis in the event of a 'No Deal' scenario.

**The UK Government's Response:**

Under the powers of the Withdrawal Act 2018, six Statutory Instruments (SIs) have been made related to SEM in order to 'remove inoperabilities relating to EU exit'. These have passed through Parliament and are ready for a 'No Deal' scenario. These SIs amend direct EU law into functioning domestic law in such a scenario.

## **2) The Future of the Internal Energy Market (IEM) post-Brexit**

The UK is currently a full member of the Internal Energy Market (IEM). The IEM enables harmonised, tariff-free trading of gas and electricity across Europe. Should the UK maintain access to the IEM, then little will change in relation to the UK's Energy relationship with the EU. However, committing to remaining fully integrated with the IEM would require the UK to comply with current and future EU Energy Market rules as well as integral aspects of EU environmental legislation.

Furthermore, to be fully aligned with the IEM, the UK would probably have to fall under the jurisdiction of the European Court of Justice. As it is the current position of the Government of the United Kingdom that the UK will leave the Single Market and the jurisdiction of the European Court of Justice, it is expected that once the UK leaves the EU it will no longer be a full member of the IEM. In addition, the UK has outlined in its technical papers that if there is a 'No Deal' scenario "European energy law will no longer apply to the UK and the UK's electricity markets will be decoupled from the Internal Energy Market<sup>4</sup>."

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<sup>3</sup> <http://www.irishstatutebook.ie/eli/2019/act/8/enacted/en/html>

<sup>4</sup> <https://www.gov.uk/government/publications/trading-electricity-if-theres-no-brexit-deal/trading-electricity-if-theres-no-brexit-deal>

**The Stated position of the British Irish Chamber of Commerce on the UK’s position within the IEM is:**

The Chamber is of the view that on leaving the EU, it would be preferable that the UK remains within the regulatory framework of the IEM. There is mutual advantage for the UK, EU and Ireland to apply and maintain consistent, coherent and coordinated policy frameworks. Maintaining coherent energy, climate and environmental policies is necessary to facilitate a balanced approach across the market, minimising the risk of inefficient distortions, such as enhancing security of supply<sup>5</sup>.

**The Stated position of Energy UK on the UK’s position within the IEM is:**

In its February 2018 position paper ‘Brexit and the future EU-UK energy relationship’<sup>6</sup>, Energy UK emphasised the need for the UK to retain close regulatory alignment with the IEM. This close alignment would also assist in protecting the SEM which the paper identified as of ‘upmost importance’. Alongside maintaining this close alignment, Energy UK have called for the UK to continue to have the opportunity to input into European energy policy, to remain in the EU Emissions Trading System (ETS) until 2020 ‘and beyond depending on future governance’ and maintain close collaboration on tackling climate change with the EU.

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<sup>5</sup> <https://www.britishirishchamber.com/wp-content/uploads/2017/04/Energy-Brochure-Web-Version-2.pdf>

<sup>6</sup> <https://www.energy-uk.org.uk/publication.html?task=file.download&id=6547>

## Roundtable Dialogue on ‘The impact of Brexit on the Single Electricity Market (SEM) and the Future of the Internal Energy Market (IEM)’

On Wednesday 27 March 2019, the British Irish Chamber of Commerce and Energy UK facilitated a Roundtable Dialogue on ‘The impact of Brexit on the Single Electricity Market (SEM) and the Future of the Internal Energy Market (IEM)’, hosted by Eversheds Sutherland, Dublin.

Attendees at the Roundtable included: UK and Irish industry stakeholders, senior civil servants, policy makers from Ireland and the UK, energy practitioners as well as members and supporters of the British Irish Chamber of Commerce and Energy UK. Specifically, the goals of the Roundtable were to:

- Discuss the issues that may arise for the SEM as a result of a ‘No Deal’ Brexit,
- Outline how potential obstructions to the SEM may be resolved,
- Consider the UK’s relationship with the IEM post Brexit, and
- Reflect on how the UK’s departure will affect the operation of the IEM.

The Roundtable was opened by Mark Varian, Chair of the British Irish Chamber of Commerce Energy & Environmental Committee and Partner, Eversheds Sutherland, who set the context for the discussion and outlined the objectives for the afternoon. This was followed by three high level addresses from:

- Michael Manley, Assistant Secretary General with responsibility for the Energy Division at the Department of Communications, Climate Action and the Environment,
- Lawrence Slade, CEO, Energy UK, and
- Dara Lynott, CEO, Electricity Association of Ireland.

*The discussion operated under the Chatham House Rule.*

The following is a summary of the main points raised by participants:

## The Impact on the Single Electricity Market (SEM)

### Continued Support of the Single Electricity Market (SEM) amongst Stakeholders

Participants at the Roundtable gave their full endorsement to the continuation of the Single Electricity Market (SEM). While not always the easiest to run, it is a concept that makes sense and has been referred to as an ‘exemplar’ at EU level and beyond. As one attendee remarked “the EU has skin in the game” on this as well and is keen to see the SEM continue. The SEM remains the most aligned market between two jurisdictions and two currencies in Europe. It was conceived before the conception of the IEM and continues to be a tangible success of North-South cooperation following the Belfast/Good Friday Agreement.

The SEM benefits the all-island market by increasing competition, enhancing efficiency and improving transparency, while also offering greater security of supply. Contributors spoke of the need to maintain the status quo as far as possible, citing that the Withdrawal Agreement, although far from perfect, was an acceptable outcome in protecting the status of the SEM. Attendees were reminded that initially the Withdrawal Agreement was to exclude ‘Energy’, however stakeholders such as Energy UK, the Electricity Association of Ireland (EAI) and Eurelectric worked together to ensure it was included as it should be seen as an opportunity for an ‘early win’ for both sides in the negotiations.

### Risks to the SEM in a ‘No Deal’ Scenario

While the SEM enjoys the support of stakeholders in Ireland, Northern Ireland, Great Britain and the EU, the reality is that a ‘No Deal’ outcome would make its implementation difficult. Under this scenario, European energy law would no longer apply to the UK’s electricity market, while the UK itself would be decoupled from the Internal Energy Market. In responding to the risk posed to the SEM by a crash out Brexit, attendees welcomed the Irish Government’s Omnibus Bill which as a contingency would allow the Commission for Regulation of Utilities (CRU) to amend licences in an effort to protect the operation of the SEM.

However, it was agreed that this legislation, although welcome, should not be considered a panacea for the SEM in the event of a ‘No Deal’ Brexit. While the Irish Government does have some reserved competences in Energy policy, the majority of energy and climate legislation is derived from the EU under the auspices of the Internal Energy Market (IEM).

As one attendee noted in their contribution “if the UK diverges on energy or climate there is very little scope for the Irish Government to respond - the SEM would be hamstrung.” Another contributor issued a stark warning that in such a scenario “the SEM would be difficult to rebuild.”

## The Potential Impact on Electricity Trading

In relation to electricity trading, the consensus in the room was that the Intraday trading and the TSO (transmission system operator) to TSO balancing market would continue as normal. However, there is no solution for the trading of interconnector capacity in the Day Ahead Market, which is currently allocated via Financial Transmission Rights (FTR) on the EU Joint Allocation Platform. Therefore, in a 'No Deal' scenario the SEM would be decoupled from the Pan-European Day Ahead Market and trading would cease at the day-ahead stage. Intraday trading would continue as this is a bi-lateral arrangement between Britain and SEM, but work would need to be done to attract liquidity to this market as most cross border trade happens in the current day ahead market. There is, however, a commitment in a 'No Deal' scenario to a consultation on proposed new trading arrangements for interconnector capacity in the Day Ahead Market, including, inter alia, a proposal to move from FTR to Physical Trading Rights (PTR).

## The Responsibility on all Stakeholders

While divergences may not exist on day one, they are likely to appear at some point in the future. So regulatory alignment will be crucial. In a hard deal scenario, it has been recognised that the maintenance of the SEM is still a key priority. Specifically, the retention of the all island local market and the intraday auctions to Britain which does not need be impacted by Brexit. There are obvious impacts for the pan European day ahead auctions between Britain and Europe & Britain and the SEM, but the SEM local market and the SEM GB intraday auctions should and can be maintained even allowing for the impacts of Brexit. Therefore, irrespective of the outcome of the negotiations, stakeholders should ensure that they collaborate as closely as possible to support the SEM including cross-border interconnection, efficient energy trading arrangements and identical climate targets.

## The Political Declaration

The Political Declaration provides a good starting point for discussing the future EU-UK relationship for energy and climate, built on alignment to ensure security of supply and efficient trade over interconnectors. It also recognises the cooperation on carbon pricing, which again will be a crucial element in ensuring a level-playing field. Regulatory alignment should also cover the climate commitments (such as Medium and Large Combustion Plant Directives, decarbonisation targets for 2030 and 2050 etc.) and financial regulation. The implementation of the newly agreed Electricity Regulation and Directive will be the first "test" of whether or not we manage to maintain the convergence.

## The Future of the Internal Energy Market (IEM) post-Brexit

The view of the Roundtable attendees was that the UK remaining part of the IEM would be the best and most logical solution for all stakeholders. However, there was an equal understanding that a leaving member of the EU cannot expect to have the same rights and enjoy the same benefits as an existing member. Finding an accommodation for the UK vis-a-vis the IEM while protecting the integrity of the Single Market will be a key challenge for the next phase of the negotiations should the Withdrawal Agreement be ratified.

### Potential Divergence

Some contributors were worried that the UK may diverge from the IEM indirectly in areas such as State Aid where the UK may choose to stimulate its economy by supporting specific indigenous enterprises. Any such divergences would create an unfair playing field between the UK and existing IEM members, therefore severing the UK's alignment with the IEM.

UK contributors countered this stating that the UK was fully aware of the consequences of a unilateral approach to State Aid rules and that such an approach would jeopardise the future trade agreement with the EU and any other potential trading agreement which the UK may wish to engage in. While in relation to climate legislation the UK has generally surpassed the EU in terms of its scope and targets and there is no suggestion that the UK would lower its ambition.

### The UK and the European Emissions Trading System (ETS)

Attendees were reminded that the UK heavily shaped the IEM as it is today and played a significant role in developing the EU law that underpins it. The UK has always been a champion of the market and competition and had significant input in promoting decarbonisation (wind, interconnectors, renewables etc.). The UK was instrumental in the development of European Emissions Trading System (ETS), which has created a level environmental playing field for energy intensive facilities across Europe.

The UK is also the second-largest emitter of greenhouse gases in Europe and its utilities and industry are among the largest buyers of permits. It is thus likely that in the UK's absence the price of EU ETS would fall. A UK contributor predicted that the likely outcome would be that the UK would introduce a UK ETS and link it to the EU's ETS, however this could not happen for at least another 18 months and therefore a partnership between the EU and UK was the only way this would work.

## Arbitration and the European Court of Justice

On the question of the European Court of Justice, UK contributors felt that a bespoke dispute resolution mechanism would need to be established in order to deal with any potential conflicts between countries, while commercial disputes would be resolved jurisdictionally. Furthermore, regulators have already indicated that primary legislation will be in place to ensure that any enforcement powers that currently exist will be replicated post-Brexit.

## Climate Targets Post-Brexit

The UK has made a significant contribution to European climate change targets. It makes sense that the UK and the EU should seek to continue working collaboratively on tackling climate change. Such cooperation between the EU and the UK on climate change and energy policies would keep costs down and increase the pace of the low carbon transition. In addition, it was voiced by some contributors that working congruently within the framework of the IEM would be necessary if the UK and the EU are to meet ambitious zero-carbon targets.

## The benefit to the EU of the UK's continued alignment with the IEM

It was felt by some that building the status quo into the future agreement would be helpful, but that it would be difficult to avoid this being seen as cherry-picking aspects of the Single Market. To maintain the status quo, the value to the EU's citizens must be proven. An example was given, that should there be an emergency situation in France, the UK can export to France via the Interconnector to ensure French electricity demand was met. It was felt important that two criteria be reached:

1. Prove the logic of the case for the UK to remain in the IEM.
2. Prove the long-term commitments to climate targets to both parties.

With the UK leaving the EU, there is potential for a different centre of gravity for the future EU policy to emerge - maybe less liberal and market-oriented and potentially more interventionist. In addition, there will be a new European Parliament and the new European Commission taking office later this year. It's not yet clear how energy and climate will position in terms of their priorities.

## The UK's Membership in European Bodies

The UK's departure from the EU will also mean that new coalitions & new relationships will be needed. It was commented that there would be a benefit to having the UK at the table but that there are certain legal impediments to this continuing. The UK's membership in bodies such as the Agency for the Cooperation of Energy Regulators (ACER) and European Network of Transmission System Operators (ENTSOs) are likely to be dependent on the exact nature of the EU-UK relationship and the statutes of both bodies, which are heavily scrutinised by the European Commission. For ACER, observatory status is the most likely outcome as ACER is strictly for EU members only. Both Eurelectric and Eurogas do allow third countries to participate. For example, Norway contributes the full EU membership rate to ensure its voice is heard. Energy UK are aiming to do the same if possible. It was also suggested that the UK needs to build stronger relationships with countries it is linked with via interconnectors.

## The Future EU- UK Relationship

A close EU-UK relationship is needed and would be mutually beneficial for both sides. Some benefits of the IEM may be replicated on a regional basis (e.g. the Day Ahead market coupling started as a regional cooperation before becoming a pan-European solution). An Irish contributor noted that from the perspective of the other 26 EU countries, there is a lot of apathy towards the Withdrawal Agreement. However, there is intense interest from the other EU members on the Future Agreement as their individual and collective interests will come into play. There is a hope that these issues can be left to technical experts, but also a fear that they may become politicised.

## The Future UK-Ireland Relationship

An attendee asked an open question to the audience on the "impact on Ireland's energy agenda on the absence of the UK from the highest echelons of the EU?" The UK and Ireland have enjoyed a mutually beneficial and cooperative relationship within the European Union structures and the UK's absence at the Council of Ministers will disproportionately impact Ireland. As one contributor articulated "if the UK is not inputting into the IEM in any guise, that is a problem for Ireland."

Ireland should ensure that UK-Ireland bilateral meetings increase and that organisations such as the British Irish Chamber of Commerce and Eurelectric are utilised more to ensure that areas of UK-Ireland interests are fed into the European discussion.