



Response to:

CPM Medium Term Review: Draft Decision Paper (SEM-11-088)

Introduction

ESB Wind Development (ESBWD) welcomes the opportunity to respond to the draft decision paper on the Capacity Payment Mechanism (CPM) Medium Term Review. ESBWD is a leading developer of wind projects throughout the island of Ireland, and the structure of the CPM, and any changes to it are of considerable importance to our business. In this response high level comments on the draft decision paper are outlined in section 1, with some specific concerns relating to some of the key changes made to the CPM highlighted in section 2.

Section 1: General Comments

Overall Change to the CPM

ESB Wind Development agrees with the general approach taken by the SEM Committee (SEMC) not to make substantial changes to the CPM at this point in time. As stated in our response to the earlier consultations on the CPM given the potential for significant change to the SEM design in order to comply with the European Target Model there is little point in making major changes to the CPM within this paradigm, with the possible consequent work and costs involved. Also the current All-Island Generation Capacity Statement 2011-2020 forecasts adequate capacity under all scenarios studied, which indicates that the current CPM is meeting its objective of providing adequate generation capacity to maintain a secure system. With these considerations in mind ESBWD is pleased to see in the draft decision paper that the SEMC propose to leave the CPM mostly unaltered.

However, there are some changes proposed in the draft decision paper which ESBWD has concerns about. Most particular of these is the proposal for the deduction of Infra Marginal Rent (IMR), which ESBWD strongly disagrees with. In section 2 these specific concerns are described in greater detail.

ESBWD agree with the RA proposal not to introduce a Capacity Credit scenario, and that all generation be treated equally as far as capacity payments are concerned. ESBWD believe that the proposed decision to maintain separate revenue payment streams for capacity payments and for ancillary services payments is the right course of action, but reiterates our opinion that the current ancillary services scheme needs to be amended to allow renewable generators to participate. We also agree with the proposal not to change the current allocation of payments.

Section 2: Specific Issues

Forced Outage Probability (FOP)

ESBWD welcome the increase in the FOP to 5.91%, as this figure is now more reflective of the outturned island-wide generator forced outage rates over the last number of years. We understand the reasoning behind having a target forced outage rate for SEM to avoid a situation where capacity may be over valued, but this revised figure of 5.91% is still some distance from the actual forced outage rates experienced, and appears to be somewhat arbitrarily chosen relative to them. With this in mind in the interests of transparency ESBWD would welcome further

explanation of this figure, in particular outlining why it is still significantly different to the actual historical forced outage rates.

BNE Calculation Methodology

ESBWD are in agreement with the proposal to fix the BNE calculation components for three years, and to index them in line with inflation annually. This proposal will improve the stability and predictability of the capacity payment revenue stream to generators. It also makes sense to do so against the backdrop of the European Target Model integration date of 2016, and any likely changes that may result of this. However, we are concerned that if the BNE calculation is not carried out in a fair manner reflective of the realities in the SEM that having a BNE in place for three years as opposed to one will only compound the difficulties faced by generators, and unfairly penalise them. ESBWD are concerned that some of the changes proposed in this draft decision paper, in particular the deduction of Infra-Marginal Rent (IMR), will have significant negative impact on generators, and that this will be compounded by having a largely unchanged BNE value in place for three consecutive years. Our concerns regarding the deduction of IMR are set out in the next paragraph.

Deduction of IMR

ESBWD strongly disagree with the proposal outlined in the draft decision paper to deduct IMR based on Option 2 as per section 7.3 of the paper. It is the view of ESBWD that Option 3 should be chosen, and the current approach be continued to measure the IMR of the BNE peaker. The Plexos runs used over the last number of years of SEM, including the 25 iterations used for the 2012 calculation have shown that the IMR supposedly received by a peaking generation plant according to the rationale applied in Option 2 does not materialise. The Plexos runs demonstrate that when peaking plants do run they set the System Marginal Price (SMP) and as a result do not receive IMR. This is the reality of the SEM, and the theoretical market equilibrium model used to justify Option 2 where IMR is deducted on the basis of the price cap and hours of lost load does not reflect it accurately. While supposedly endeavouring to reduce capacity payment volatility, the introduction of this proposal would needlessly introduce additional volatility (i.e. the consequent reduction in capacity payment revenues due to the change), while relying on a dubious theoretical calculation.

A consequence of the deduction of this “notional” IMR will be a significant reduction in capacity payments to all generators. This amounts to an unfair penalty on all generators participating in the market. The example given in the draft decision paper to demonstrate Option 2 shows a reduction in the BNE cost of almost 9%, which would have a considerable impact on generator capacity payment revenues. ESBWD believes that the status quo should be maintained, i.e. Option 3 should be chosen instead of Option 2.

Flattening Power Factor (FPF)

The draft decision paper proposes to increase the FPF from 0.35 to 0.5 in 2013. ESBWD would prefer to see this factor remain at 0.35 rather than see it be increased to 0.5. The proposed increase would result in greater capacity payment volatility, and more unpredictable capacity payment revenues for all generators. This is contrary to the price stability objective of the CPM. While all generators would be affected by the greater volatility, renewable generators would be especially affected by the proposed change, as capacity payments would now be weighted more heavily towards periods

of low wind. This amounts to an unfair penalty on non-dispatchable wind generators, which is contrary to the principle of fairness described in the objectives of the CPM.

WACC Calculation Methodology

In the draft decision paper there is no change to the WACC methodology. ESBWD disagrees with this, as in the view of ESBWD the use of UK figures for the Northern Ireland rates are incorrect in the context of an island wide market. This results in too low a figure for the WACC. Rates more reflective of actual Northern Ireland rates should be used to more realistically reflect all-island rates.

If you have any questions or would like to discuss any of the matters raised further please contact:

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