NIE Energy Limited
Power Procurement Business (PPB)

Treatment of Losses In the SEM

Consultation Paper

SEM-11-098

Response by NIE Energy (PPB)

27 January 2012.

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Power Procurement Business

Introduction

NIE Energy – Power Procurement Business ("PPB") welcomes the opportunity to respond to the consultation paper on the Treatment of Losses in the SEM that seeks views on the analysis conducted on the impact of TLAF splitting.

Interpretation of the results of the impact assessment

The results will inevitably reflect the TLAFs used and PPB has previously expressed concerns with respect to the locational TLAFs derived for 2008 and 2009, as they were determined on the basis of higher assumed generation levels on Northern Ireland generating units (and hence higher North-South energy flows) than we were forecasting at the time, and also that were much higher than actually outturned. As a result of the TSOs' assumptions, NI generators were allocated lower average TLAFs than generators in RoI in these years. This anomaly may be a reason for the slightly counter-intuitive results determined for 2008/09 and 2009/10 in respect of Total Production Costs (as shown in Table 1 and Graph 3 in the consultation paper). The locational TLAFs determined by the TSOs for 2010 were more reflective of both forecast and actual despatch and therefore we consider the results for 2010/11 to be more robust.

The results for each of the TLAF scenarios for 2011/12 that include the East-West Interconnector are difficult to comprehend since, for example, they show higher production costs and higher customer costs, when the expectation would be that costs should decrease or, at worst, remain neutral following the introduction of the East-West interconnector.

The results are considered below for each of the SEMC's assessment criteria.

Stability of the Market Schedule

The analysis clearly illustrates that the consequence of moving from locational TLAFs to Uniform TLAFs is to transfer inframarginal rent and hence profit from generators in Dublin and Northern Ireland (where the generation is located close to, and/or balanced with, demand) to generators located in Cork who are located in a poor network location.

Production Efficiency

As we outlined earlier, we consider that there were flaws in the TLAFs that were applied in 2008 and 2009 and hence this may be contributing to irrational results for the 2008/09 and 2009/10 years. Similarly, the "2011/12 (EW)" results which show higher production costs following the introduction of the East-West interconnector are counter-intuitive and therefore may be unreliable.

The results for 2010/11 and 2011/12 (w/o EW) show that while the production costs are relatively close across the TLAF scenarios, there is a progressive increase in costs as you move from locational TLAFs to Uniform TLAFs which is what one would conceptually expect.

Constraint Costs

For the same reasons as outlined previously, we consider that the 2010/11 and 2011/12 (w/o EW) are the most reliable years to consider and again the analysis shows that using Locational TLAFs for both Dispatch and the Market schedules results in the lowest constraint costs. This is again consistent with what logic would suggest should be the outcome since if you artificially schedule generation in poor network locations through the use of a uniform TLAF, then the cost of constraining those generators down or off and constraining others on effectively crystallises the economic inefficiency for customers through the constraint costs.

Impact on the all-island customer

Again, we discount the 2011/12 (EW) results as, against any reasonable expectation, the analysis shows costs increasing as a result of the investment. At the very worst, the interconnector would remain unused and the costs should be the same as they would in the case without the interconnector. Hence there appears to be something awry with the modelling in that scenario.

Similarly, although we have reservations over the first two years (as previously expressed), the results lead to a reasonably consistent conclusion for the years 2008/09 through to 2011/12 (w/o EW), showing that the use of Locational TLAFs for both Dispatch and the Market provides the lowest cost outcome for customers, while the use of Uniform TLAFs for both schedules results in the highest costs.

Divergence between the market schedule and dispatch schedule

It is not clear what value the analysis of the energy (GWh) variance between the dispatch and market schedules adds. The critical consideration, as noted in section 3.4, is the impact on overall constraint costs which is set out in section 4.3 of the consultation paper, and upon which we have commented above.

We would also note that there would normally be a reasonable correlation between the GWh variance and the Constraint Cost (i.e. cash) variance. There are some odd exceptions that can be seen from a review and comparison of Table 2 and Table 8. For example, in Table 8, the energy variances are greatest between Locational Dispatch and Uniform Market scheduling (as would be expected), yet this is not reflected in Table 2, and in particular for 2011/12 (w/o EW) where the constraint cost is the lowest of all the TLAF scenarios in the year.

What is the appropriate treatment of losses?

The analysis generally substantiates what logic would indicate, confirming that the use of Locational TLAFs for both the determination of the Market Schedule and in Dispatch consistently delivers the most efficient dispatch, the lowest level of constraint costs, and the lowest costs for customers. In addition it also avoids an arbitrary reallocation of revenues from generators who are located in a good network location to those in a poor location, thereby ensuring there is a signal that rewards investment in the correct location.

PPB sees no value in splitting the use of TLAFs. The costs are generally increased for customers and there would be further system costs, for both the TSOs and generators to operate and monitor the arrangements. It is also unclear how such a divergence would be compatible with the new wholesale arrangements that will be adopted to enable compliance with the regional integration requirements and alignment with the EU Target Model.

PPB considers that the most appropriate solution for TLAFs is to revert to the use of Locational TLAFs and that there is absolutely no case for adopting uniform TLAFs. We note that the cost differentials for production efficiency and customer costs between Locational and Compressed TLAFs are generally small (<1%). However, the decision has a greater impact on the re-allocation of Infra-Marginal rent and it is not clear why the SEMC should arbitrarily determine that Cork generators should be subsidised by other market generators (as is evident from Graph 1).

To the extent that the SEMC may determine that there is little difference between Locational and Compressed TLAFs, in terms of production efficiency, constraint costs and consumer costs, it would be appropriate for the SEMC to avoid distortion in the allocation of Infra-marginal rents that affects the profitability of generators and should not seek to support generators located in poor locations by improving their TLAFs through compression.