

ESB Response to Incentivisation of All-Island Dispatch Balancing Costs

Introduction

ESB welcomes the opportunity to respond to the SEM Committee consultation paper on “Incentivisation of All-Island Dispatch Balancing Costs”. The timing of this consultation has coincided with a number of other important papers issued to the market: “CER Decision on 2011/2012 Transmission Incentives” and SEM Committee consultation paper on “Imperfections Charges for October 2011 – September 2012”.

It has been estimated by the TSOs that Dispatch Balance Costs (DBC) will be circ. €143m for 2011-2012. The introduction, at the earliest opportunity, of an incentive mechanism on the TSOs to manage DBC would be beneficial for all consumers.

While many of the factors that give rise to DBC are, to varying degrees, outside the control of the TSOs (EirGrid and SONI), they do have the ability to effectively manage a number of the causal factors and ESB believes that it is appropriate that TSOs be incentivised to do so.

All-Island DBC Incentive Proposal

ESB supports the introduction of an All-Island DBC incentive, provided such incentive doesn't as a consequence introduce unintended outcomes which impact on the effective operation of the SEM.

ESB believes that for any DBC incentive to be effective, particularly should the incentive be measured against the TSOs own forecast of DBC, that as a first step each year, a robust challenge of TSOs DBC forecast needs to be performed. The incentive mechanism could then be structured to minimise the scale of DBC over time rather than just beating the forecast each year.

Recognising that some of the DBC causal factors are either completely or partially outside the control of the TSOs, ESB agrees that the incentive mechanism should incorporate asymmetric parameters and appropriate dead-bands in order to cater for these varying levels of control. In addition, any ex-post review would need to consider all high impact low probability events and assess the level of control that the TSOs had over their occurrence or impact on DBC.

Notwithstanding this, ESB believes that a set of stretching targets can be set for the TSOs each year.

At present, dispatch decisions taken by the TSOs are not transparent to the industry. ESB believes that such transparency, brought about through regular reporting by the TSOs on dispatch decisions and DBC must be established as soon as possible. ESB suggests that this reporting incorporates (no less frequently than) quarterly and year-to-date DBC data supplemented by information identifying all causal factors and the rationale behind any key associated TSO dispatch decisions.

Incentivisation against an Assumed Rule Set

ESB suggests that the DBC incentive mechanism introduced is done so with recognition of the SEM market rules as approved. As the market rules change over time, for example to reflect intra-day trading, then the incentive mechanism would need to be revised.

In addition, ESB suggests that the incentive mechanism be designed in a manner that doesn't promote TSOs to seek changes to the market rules as they operate today, in order to support TSO profit maximisation at the expense of market participants' revenues. For example, ESB suggests that the incentive mechanism is designed in a manner that doesn't simply result in the transfer of balancing costs from the TSOs to market participants through new charges or penalties, rather than reducing the causal factors.

Factors Influencing DBC

ESB is of the view that the high level of intermittent generation, together with the necessity for the TSOs to retain an appropriate amount of operating reserve on the power system will continue to give rise to some level of constraint costs within the SEM.

EirGrid has identified a number of factors that can cause DBC to increase, each of which, to some extent, is within the TSOs control to manage. ESB believes that there is some scope for incentivising the TSOs to improve performance and by consequence service to the market in the following areas:

- **Transmission reinforcement:** Completion of the North-South Interconnector will ease constraints on the whole power system. However, as a set of Transmission Incentives has already been decided on by CER, and are under consideration by the Utility Regulator for the north, a separate or duplicative mechanism under DBC to achieve the same result does not seem appropriate;
- **(Lack of) Perfect Foresight:** ESB is of the view that in the absence of a complete set of real time information to the TSOs that "perfect foresight" will continue to remain elusive when dispatch decisions are being made. Notwithstanding this, ESB supports the introduction of incentive mechanisms on the TSOs to improve the accuracy of system demand forecasting and wind forecasting, in order to improve the accuracy of information for dispatch and market trading purposes;

Summary

ESB supports the introduction of an incentive mechanism for the TSOs to manage and reduce DBC. This incentive mechanism if successfully introduced for tariff year 2011/2012 will provide early benefits to the market.

However, the incentive mechanism must be designed in a way that doesn't introduce unintended outcomes which impact on the effective operation of the SEM. Similarly, the net result of any incentive on TSOs to manage dispatch balancing costs must not result in a series of changes to the market rules or a new set of charges or penalties for

market participants, either of which would just be a direct transfer of risk from the TSOs to the market. The incentive mechanism needs to be designed so as to give rise to initiatives by the TSOs that manage and reduce the DBC causal factors that are either totally or partially within their control.

Transparency of TSO dispatch decisions and their impact on DBC, together with other causal factors will be necessary in order for the success of any incentive mechanism to be evaluated. Reporting by TSOs on dispatch decisions is required as soon as possible.

ESB supports the introduction of incentives on TSOs in areas such as system demand forecasting and wind forecasting where improvements would assist TSOs with DBC management as well as provide additional value to the market.