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Subject: Incentivisation of All Island Dispatch Balancing Costs

Dear Jamie/ Billy

The NEAI welcomes the opportunity to respond to SEM-11-048: Incentivisation of All Island Dispatch Balancing Costs consultation paper.

The National Electricity Association of Ireland (NEAI) represents a broad cross-section of the electricity generation and supply sectors on the island of Ireland. Our mission is to contribute to the development and competitiveness of the electricity industry on the island of Ireland by representing the interests of our members at national and European levels and to advance the role of the electricity industry in support of social and economic development.

NEAI is broadly supportive of the RAs proposals. We support the principle that electricity TSOs should be incentivised and would also suggest that the same principle should apply to gas TSOs particularly in the context of an all island CAGSO. For electricity we believe that it is important to implement an incentive for the key area of dispatch balancing costs (DBC) and that this should operate on an All Island basis. The structure of the incentive should be mindful of unintended consequences and should avoid competing with TSO system security obligations while taking into account where possible material factors beyond the TSOs' control. The proposed structure is a good starting point that will no doubt require adjustment in future, based on experience, but it is important to start now with a trial incentive.

We comment below on the specific issues posed by the consultation:

Applicability of an All-Island incentive mechanism in the Current Industry Structure

NEAI believes that the incentive can be applied within the current industry structure. NEAI agrees that incentive design using deadbands and asymmetry can accommodate any issues arising from industry structure. As experience develops, the separate incentives for the network owners (e.g. in capital work) can be adjusted in a complementary way as proposed. Where these are not in place, they should be urgently introduced.

How such an incentive may be introduced:

NEAI would propose that the incentive be introduced to coincide with the October 2011 to November 2012 payments. We believe that implementation will depend on experience and further analysis at this point will not necessarily lead to a better answer. DB costs are increasing. In addition to the factors highlighted by EirGrid such as increasing wind penetration, greater interconnection and intra-day trading are also likely to exert upward pressure on constraint costs. The observed increase in DB costs means that there is a case for introducing a worthwhile incentive now rather than later, albeit it is important to be mindful of unintended consequences, system security obligations and the need for greater transparency.

Monitoring of DB costs

We agree with the RAs proposal for the TSOs to develop a report template for regular reporting on the costs and the constituents of the costs as well as drivers, trends and TSO actions. Reporting should commence immediately as this is not dependent on the introduction of incentives.

We agree that transparency should be a key consideration; TSOs should provide detail on the rationale for constraint dispatch decisions and identify the causes of constraining generators on or off. Frequently published updates on the TSOs' websites of the Transmission Constraint Groups Report would also be necessary.

The design of and parameters/rewards/penalties of such a mechanism

We believe the design set out in Figure 5 in Section 3 is a strong starting point for the mechanism. The key issues are:

- (a) Provide an incentive to the TSOs that makes the management focus and any necessary changes worthwhile.
- (b) Ensure that external factors are allowed for.
- (c) Provide sufficient flexibility for the future.

The proposed mechanism addresses the above issues in our view. In addition, further consideration of the three key respects detailed below may be required:

- (a) The incentive should be based from the outset on gross DB costs (i.e. before other charges are netted off) as this is necessary to avoid duplication of incentives that already exist on other parties through other system charges.
- (b) The incentive should not compete with or compromise TSO security of supply obligations, for example in the context of capacity tests for system security.
- (c) The incentive should be linked to the current market rules. A materially relevant change in rules should not of itself lead to penalties or benefits for the operators.

The NEAI also supports the complementary proposal to set an incentive for wind and demand forecasting. This incentive might be set on the percentage difference between forecast and actual wind and demand, utilising the bounds proposed in Figure 5 of the consultation paper.

However, targets should not be set by the TSOs themselves, and performance should be rigorously assessed by the RAs.

Ancillary services

While the consultation does not deal with the issue of incentivisation of ancillary services we believe that the SEM Committee should address the requirement for and incentivisation of ancillary services as a matter of urgency in order to support the increasing level of wind penetration in the SEM. Incentivising DB costs and ancillary services are not mutually exclusive and incentives on both will better facilitate the reduction of constraint costs across the system.

Conclusion

NEAI broadly support the RAs proposals and look forward to their implementation subject to the necessary considerations highlighted in this response.

Please do not hesitate to contact me if you wish to discuss this further.

Yours sincerely,

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