

Incentivisation of All-Island Dispatch and Balancing Costs

Synergen's response to SEM-11-048

1 Introduction

This paper is Synergen's response to the consultation paper "SEM - Incentivisation of All-island Dispatch Balancing Costs" (SEM-11-048), published on 23rd June. Synergen has no objection to this response being published.

2 Observations on the background section

The consultation sets out a number of factors for consideration regarding the possible introduction of incentives on the TSOs to reduce dispatch costs – such costs being primarily the costs associated with constraints. These are commented on below.

2.1 Dispatch Balancing Costs (DBC's)

Synergen notes that DBCs are a significant cost, and that a number of factors (primarily fuel costs and long term forced outages) have led to these costs being significantly higher than forecast in SEM-10-055, thus requiring upwards adjustment to the 2011/12 imperfections charge K factor.

Synergen strongly concurs with the EirGrid observation referenced in the paper that such costs are due to the SEM design. In this context, Synergen notes that the RAs specifically adopted an unconstrained market schedule backed by financially firm access for most generation. The rationale for such a design must be that the benefits of competition on an unconstrained basis outweigh the cost of constraints¹. In this context, significant constraint costs are not unexpected, and thus the application of incentives on those best able to manage such costs downwards is necessary and appropriate.

The transmission incentive arrangements in BETTA are longstanding, with their genesis in the early 1990s. The original UMIS arrangements from 1994 have evolved from incentive based hedges against specific elements of Uplift² (of which the major element was the cost of constraints) into the price control framework. Against this backdrop, Synergen considers that the efficient operation of the SEM from 2007 to date, would have been enhanced through the earlier adoption of measures along the lines now being suggested.

2.2 Incentives

There are conflicting views regarding incentives between the TSOs and market participants. Synergen notes that the TSOs consider incentives are not appropriate as (a) the TSO / TAO split reduces the TSO influence over costs, and (b) the TSO's have a

¹ Synergen's response to the RAs preferred market design suggested price separation when constraints bound – essentially a market that set one price when unconstrained, by transmission, and more than one price when constrained.

² Note – Uplift in the E&W Pool was not equivalent in its elements to Uplift as defined in the T&SC in the SEM, being closer to, but not exactly the same as, Imbalance Charges.

limited ability to control dispatch costs. Synergen does not accept this view, and notes that:

- Notwithstanding the TSO / TAO split, the TAO could apply contractual incentives to the TAO, if TAO actions substantially drove costs in areas outside of the TSO control;
- The experience of UMIS in the E&W Pool demonstrated that grid system management actions (the TSO function) was a major driver of constraint cost reductions; and
- The incentives on NGC led to considerable innovation by NGC, which in the absence of the incentives would not have been developed. In short, in the E&W Pool, the NGC's grid operation drove some constraint costs, and these were reduced by BOTH refinements to dispatch efficiency, and new working approaches to grid maintenance scheduling and timing. These changes moved the situation from one where NGC would not (pre UMIS) incur £1,000 of costs to reduce £1,000,000 of Supplier costs through higher Uplift, to one where the actions of the Grid and customers were increasingly aligned.

In this context, there is a lack of transparency in the SEM dispatch process, which in Synergen's view exhibits elements of subjective judgement rather than a transparent, auditable cost minimisation. It is also notable that the TSOs are very pro-active about the application of "incentives" to generators, which are all stick and no carrot and include penalties in events where the generator has no direct control (e.g. short notice re-declaration penalties). In contrast, the EirGrid proposals on Outturn Availability on which it recently consulted, were notably short on any incentives on the TSO to undertake connection asset maintenance efficiently – leaving the consequences of the asset being unavailable squarely with the generator, and if the maintenance over-ran the market itself. Compared to the "incentives" it imposes on generators, the proposed arrangements for the TSO's are benign.

3 Proposed structure and the setting of the incentive targets

Synergen believes that the structure for the proposed incentive design set out in Section 3 of SEM-11-048 is, in principle, appropriate and workable. However, the setting of the parameters and sharing factors needs to be undertaken on the basis of demonstrated analysis of the level of controllable costs, and their drivers. At this stage, therefore, the bands and sharing factors cannot be commented upon. Synergen believes that for the setting of the incentives it may be appropriate for the RAs to consider the type of arrangements that were developed in the E&W Pool, but also the process by which the original UMIS sharing factors and strike prices were developed. Synergen thus suggests:

- The Suppliers negotiate the structure and strike prices with the TSOs with the RAs having oversight over the negotiations; and
- The TSOs provide the Suppliers with analysis of historic dispatch costs, their dispatch process, and modelling of future costs to facilitate these negotiations.