19th November 2012

Jamie Burke
Commission for Energy Regulation
The Exchange
Belgard Square North
Tallaght
Dublin 24

Dear Jamie,

RE: Proposed Decision on the Treatment of Curtailment in Tie Break situations, SEM-12-090

Bord Gáis Energy ("BG Energy") welcomes the opportunity to respond to the Proposed Decision on the Treatment of Curtailment in Tie Break situations ("the Proposed Decision").

BG Energy commends the SEMC's engagement with industry participants in re-opening the SEM-11-105 decision and trusts that industry views are given due consideration when forming the final decision on this important issue. The Proposed Decision to disregard the 'Grandfathering' option to apply curtailment based on the level of firmness of a wind farms network connection is welcomed. However, although BG Energy agrees with the proposal to allocate wind curtailment on a pro-rata basis, it disagrees strongly with the phased removal of all compensation for wind generators for curtailment.

1. Introduction

BG Energy contends that the Proposed Decision is based on a flawed analysis regarding the benefits to consumers that removing curtailment revenues would bring. BG Energy believes that any consumer benefits must be viewed in context of overall Dispatch Balancing Costs (DBCs) and indeed total energy costs to which consumers are exposed. Any benefits must also be contrasted with the risks that increased regulatory uncertainty could lead to lower wind development, reducing the benefits to consumers that high levels of wind generation delivers in terms of reduced energy prices and emissions.

In BG Energy's view, the Proposed Decision to phase out market revenues for curtailed wind generation amounts to a retrospective change, which removes revenues that generators have a legitimate expectation to receive. This will create considerable regulatory and investor uncertainty at a time when significant levels of investment are required to meet renewable targets. Furthermore, given the SEMC's previous decision (SEM-11-084) with respect to a threshold for material harm to consumers has not been demonstrated, the issue of curtailment compensation should not be addressed at this time.

BG Energy commends the work done to date in establishing curtailment mitigation initiatives such as the DS3 Programme. The delivery of these initiatives is essential if the benefits of wind generation are to be maximised for all-island consumers and if curtailment levels are to be effectively managed on the system. However, it must be recognised that the delivery of these mitigation measures is beyond the sole control of wind developers. While wind and conventional generators have a role to play in the delivery of DS3, the risk of curtailment should sit with the parties that can best influence it currently, i.e. the System Operators. On that basis, no changes to market arrangements for curtailment should be considered until mitigation measures are delivered and the current target of maximum System Non-Synchronous Penetration (SNSP) level of 75% is achieved.

This response will now comment on the significant aspects of the proposed decision before addressing the requirements for transparency around the operation and reporting of curtailment and finally summarising with key messages.

2. Comments on the Proposed Decision

BG Energy agrees with the conclusion drawn by the SEMC in the Proposed Decision that under 'Grandfathering', non-firm wind projects would not proceed due to punitive levels of curtailment making the achievement of renewable targets very unlikely if not impossible.

BG Energy also agrees with the pro-rata approach that allocates curtailment equally between all wind farms, regardless of the level of firm connection they have. Sharing the burden of curtailment among all wind farms is the fairest solution given that it has been clearly established that curtailment is a system-wide issue and bears no relation to network and location specific issues.

However, BG Energy strongly disagrees with the removal of curtailment market revenues for eligible generators. BG Energy asserts that the analysis that underpins the Proposed Decision is incomplete and this retrospective change removes revenues from wind generators who have a legitimate expectation to receive them. A combination of these factors significantly increases regulatory and investor uncertainty, damaging the ability of wind developers to finance viable projects and thus the delivery of a fundamental pillar of energy policy in Ireland and Northern Ireland, the 2020 renewable targets.

2.1. Concerns regarding the Analysis

BG Energy believes that the decision to remove market revenues for curtailment is based on an incomplete analysis of the costs and benefits of such a proposal and is therefore flawed. The Proposed Decision considers curtailment revenues an *"undue and inappropriate burden on the all-island consumer"* that should be removed. BG Energy does not agree with this assertion and believes that existing market revenues for curtailment are neither undue nor inappropriate and are a core feature of the SEM market design that must be retained.

The Proposed Decision states that the benefit of removing payments for curtailment for the all-island consumer will amount to approx. €13 million in 2020 and these financial benefits to the consumer have been used as the rationale behind the SEMC's Proposed Decision. BG Energy is concerned that the purported benefit is based on flawed methodology applied in the analysis. Specifically, the **reference case from which the benefit was measured compensates ALL**

wind generation for curtailment (both firm and non-firm)[1]. However, current market rules dictate that only firm wind generation receives compensation. BG Energy believes that in no instance will all wind generation be firm by 2020. Therefore, a more accurate view of the estimated consumer benefit in 2020 would be the difference between the current arrangements for compensation (Option 2 in TSO modelling) and the savings if compensation is removed (Option 4 in TSO modelling). This reduces the benefit to approx. €9 million in (i.e. the difference between Option 2 and Option 4 in the TSO modelling). If the consumer benefit is to be used as a rationale for the decision on the treatment of curtailment revenues, this should be based on market realities as opposed to using unrealistic assumptions regarding network build-out and therefore firmness in 2020.

BG Energy is concerned that while the impact of the Proposed Decision has been assessed from a DBC cost viewpoint, other costs and benefits have been largely ignored. In responding to queries raised by industry, the TSO has confirmed that curtailed wind was removed from the market schedule in the course of its DBC modelling. However, the impact this would have on the SMP was not included in the modelling results presented. BG Energy believes that if wind is excluded from the market schedule, it is likely to increase SMP as more expensive marginal plant then sets the price. BG Energy contends that the **impact of any changes to SMP and the treatment of curtailed wind generation in relation to the market schedule must also be considered by the SEMC** in this decision, as any perceived benefit from reduced DBC costs could be outweighed by increases in SMP.

In conclusion, BG Energy believes that although the TSOs analysis shows that there may be a marginal benefit at best for all-island consumers by removing curtailment generator revenues, through reduced DBC costs; this could be outweighed considerably by reductions in SMP due to higher levels of wind generation in the market schedule, which is omitted from the TSOs analysis. Furthermore, any benefit must also be assessed in terms of the cost of damaging investor certainty at a time when unprecedented levels of investment are required in wind generation. Because of the incomplete nature of the analysis of consumer benefits of the Proposed Decision, BG Energy believes that all-island consumers are best served by retaining the existing market arrangements for curtailed generation, thereby benefiting from increased wind penetration and lower market energy prices associated with the achievement of the 2020 renewable targets.

2.2. Retrospective Changes to SEM and Regulatory Uncertainty

BG Energy considers that the Proposed Decision to remove curtailment revenues amounts to a **retrospective change to a fundamental element of the SEM design** that substantially increases regulatory and investor uncertainty. For renewable energy targets to be met, it is estimated that between 350-400 MW of installed capacity is required each year between now and 2020. The size of the challenge is considerable, given that the SEM has yet to see this scale of build-out. If this challenge is to be met, BG Energy believes that the Regulatory Authorities must seek to minimise regulatory and investor uncertainty by rejecting the proposal to remove curtailment revenues.

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[1] See p5 of SEM-12-090a (Effect of Tie-break Options on DBC and Curtailment, Eirgrid)

The provision of market revenues to firm generators in the event of an instructed reduction in output is **one of the High Level design principles of the SEM**. Implementing this change effectively removes an existing wind generation revenue stream, one which wind developers have a legitimate right to expect to continue. To change such a principle as per the Proposed Decision is to fundamentally change the market and to contradict the SEM Committees proposal in its latest consultation paper[2] that it will not seek to make material market changes until such time as the Target Model solution is designed.

The removal of this market revenue for curtailed firm wind generators represents a **retrospective change** and is, in BG Energy's view, very damaging in terms of long term regulatory and investor certainty. Not only will it directly damage the financial viability of current and future wind developments by removing an existing source of market revenues, it will also have indirect negative effects by increasing the risk premia demanded in project financing arrangements. This will further hamper future projects in the SEM by adding to the cost of financing.

2.3. Demonstration of 'Material Harm'

In October 2011 the SEMC stated that *"no fundamental changes to the SEM High Level Design are envisaged in the interim period unless they are clearly warranted on grounds of* ***'material harm'*** *to end customers"* as part of their decision on Monitoring the Divergence of the Market Schedule from Dispatch and the Impact on Consumers[3].

This decision stated that four metrics would be monitored to measure the level of 'material harm' to consumers (constraint payments, proportion of energy payment attributable to constraints, infra-marginal rent earned as a result of being constrained off and constrained running by volume (divergence)). No reference is made to the 'material harm' decision in the Proposed Decision and BG Energy is concerned that this decision has not been considered in the consultation process on curtailment to date.

BG Energy considers that the 'material harm' decision should receive due attention by the SEMC in finalising their decision on curtailment revenues. Given that the levels of DBC benefits that may accrue by the removal of curtailment revenues are not considered significant by the TSO's, BG Energy believe that **'material harm' cannot be demonstrated** and as such, current market arrangements relating to curtailment should be retained.

2.4. Implications for Market Design

BG Energy believes that SEMC must consider the **impact that European Regional Electricity Market Integration will have on regulatory uncertainty in the SEM** in the coming years given the requirement to be compliant with the European Target Model by the end of 2016. All generators face increased uncertainty because of likely changes to the SEM and none more so than wind generators, who face additional uncertainty including the treatment of balancing requirements, priority dispatch and support mechanisms.

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[2] See p18 of SEM-12-105a (Market Integration Next Steps Proposed Decision Paper)

[3] See p3 of SEM-11-084 (Monitoring the Divergence of the Market Schedule from Dispatch and the Impact on Consumers)

A transparent process for the design and delivery of any changes to the SEM is essential if all stakeholders' requirements are to be met as optimally as possible. Consequently, BG Energy is concerned that the Proposed Decision will result in the **de-facto establishment of a design principle of the SEM post-regional integration**, namely that wind generation is not entitled to the same rights regarding firm access to the network as other forms of generation are.

BG Energy believes that the treatment of wind in the post-regional integration SEM requires due consideration by all stakeholders in the appropriate forum and not as part of this decision. BG Energy reiterates the need for regulatory certainty to be delivered by retaining current market arrangements for firm generators.

2.5. Entry Signals

It is clear that significant investment is required in wind generation if energy policy goals are to be met. A crucial element of attracting the requisite investment is an efficient entry signal. BG Energy considers that the pro-rata treatment of curtailment sends an efficient entry signal for wind developers to connect to the system compared to grandfathering.

The removal of curtailment revenues dilutes the entry signal for wind generators and would increase the unpredictability of the regulatory environment and hamper the ability of projects to achieve financing. For this reason, BG Energy is of the opinion that the additional removal of market revenues for curtailed wind generation does not strengthen the entry signal and should be rejected.

3. Transparency

BG Energy has concerns regarding the lack of transparency in the reporting of constraints and curtailment events and the delivery of curtailment mitigation measures. In addition, transparency concerns include the annual DBC forecast submitted by the System Operators and approved by the Regulatory Authorities, the composition of which is not shared with industry. BG Energy believes that these transparency issues are key elements in the treatment of curtailment and must be considered in the final decision on this matter.

The Proposed Decision acknowledges that curtailment is not associated with network specific issues and that constraints and curtailment are two different situations with differing causes. The previous consultation on curtailment raised a concern around the practical implementation of applying different rules to constraint and curtailment events. The introduction of an Operational Rule set such as that proposed by the TSO's in SEM-12-090b and the confirmation that Eirgrid can implement such a rule set alleviates this concern. To this end, **BG Energy supports the introduction of the proposed Operational Rule set distinguishing constraints and curtailments**.

Nevertheless, wind generators require far greater transparency around the reporting of constraints and curtailment than is currently being provided. The 2011 Curtailment Report prepared by the System Operators has yet to be officially released publicly by the Regulatory Authorities, months after its completion. This report is required on a more frequent basis and with far greater detail to demonstrate to investors that current and future issues that cause curtailment are being addressed effectively.

The removal of curtailment revenues means the operational actions of the System Operators will have an even greater financial impact on wind generators. Therefore, wind generators will require, and indeed request, more detailed and frequent information from the TSOs in relation to curtailment actions taken. For this reason, it is incumbent that the System Operators publish reports that show how and where curtailment is being applied and the progress in delivering mitigation measures such as the DS3 Programme.

DBC costs for the current tariff year 2012/2013 are in the order of €140 million, nearly all made up of constraint costs (that include the costs of curtailment payments). DBCs are caused by deviations between the market schedule and the dispatch schedule. While a certain amount of deviation is unavoidable to ensure the secure and reliable operation of the system, other sources of deviation can be addressed by the System Operators such as the non-delivery of network infrastructure and efficient network operation. BG Energy considers that there is a lack of transparency around what, specifically, these costs are comprised of. The composition of DBC costs must be made more transparent because of the material difference they make to costs of consumers and to the revenues of generators.

4. Summary

BG Energy recognises that the SEMC's primary objective is the protection of consumers throughout the all-island market and that this objective sits alongside national energy policy goals to achieve 40% renewable penetration by 2020.

With these objectives in mind, BG Energy agrees with the pro-rata approach to the allocation of curtailment as the most equitable solution to what is a system-wide issue. However, BG Energy strongly disagrees with the Proposed Decision to remove curtailment market revenues for eligible generators for the following reasons:

- It is based on an incomplete analysis of the consumer benefit of removing curtailment revenues and does not consider the cost through impact on SMP, nor the significance of the benefit in terms of the overall DBC and energy costs that the consumer faces.
- It introduces significant regulatory and investor uncertainty by applying a retrospective change to current market arrangements in a time where significant uncertainty exists due to the forthcoming European regional integration and where considerable investment is required to meet renewable targets.
- It has not demonstrated that curtailment payments amount to 'material harm' to consumers and, as such, does not have due justification to make a fundamental change to the SEM at this time by removing curtailment payments.
- It removes a source of revenue from generators that have legitimate expectation to receive it and where investment has been made and projects are operational or are at a stage of significant development, adding to regulatory uncertainty.

- It transfers the financial risk of non-delivery of curtailment mitigation measures such as the DS3 Programme from the System Operators who can influence their delivery, to wind generators who cannot.

As already stated, BG Energy disagrees with the proposal to remove market revenues for curtailment. The removal of compensation before mitigation measures are delivered is an unfair transfer of risk onto wind generators given the lack of transparency around curtailment reporting and DBC costs that currently exists.

For curtailment mitigation measures to be delivered as efficiently as possible, a clear signal must exist for those that can influence their delivery, the System Operators. Appropriate curtailment payments are such a signal and should be retained. Any removal of compensation can only be considered when material harm has been demonstrated AND when system wide mitigation measures and an SNSP level of 75% have been delivered.

In conclusion, BG Energy believes that the SEMC's objectives to protect consumers and to facilitate renewable development in the SEM can be met most effectively by applying pro-rata allocation of curtailment and retaining current market arrangements in relation to revenues due to curtailed generation.

Please do not hesitate to contact me should you wish to discuss any of the issues raised in further detail.

Yours sincerely,

Ciarán O'Brien
Regulatory Affairs – Commercial
Bord Gáis Energy

{By email}