

Submission by Bord na Móna PowerGen

to the

SEM Committee Consultation Paper

**Treatment of Gas Transportation
Capacity Costs**

SEM-12-089

Introduction

Bord na Móna (BnM) welcomes the opportunity to respond to the SEM Committee's consultation paper on the 'Treatment of Gas Transportation Costs Criteria' - SEM-12-089.

From the outset, Bord na Móna acknowledges that the company does not currently generate electricity using gas as a feedstock. However, as a market participant and given the fundamental nature of this Consultation relating as it does to the Bidding Code of Practice (BCoP) and how value should be attributed to a cost item being 'bid-in', BnM feels obligated to comment on principle.

At a high level, Bord na Móna would advocate that gas markets on an all-island basis are sufficiently developed to require gas generators in the SEM to include the cost of short term gas transportation within their Commercial Offer Data (COD). Furthermore, the value attributed to this cost should simply be based upon the regulated cost of the daily product and that thirdly, for the purposes of clarity, the Annual Capacity Payment Sum (ACPS) should not be re-opened and adjusted as it appears that the Best New Entrant (BNE) would continue to be a dual-fuel unit even after treating gas transportation capacity as a non-fixed cost element. In the following sections the rationale for the conclusions reached in the above paragraph are discussed.

Has there been sufficient development of the gas transportation capacity market to allow costs to be included in bids.

At a high level, the availability of 'daily' products implies that the cost of gas transportation is not fixed and that the total cost faced by a generator is not the same irrespective of whether or not the unit was operating or not. This conclusion requires that such costs be therefore included in the COD for prices to comply with the SEM's 'Cost Reflective' bidding principles.

The Consultation paper differentiates, for the purpose of including Gas Transport costs in COD, units based in RoI *versus* units located in NI, however, the paper does welcome comments on this stance.

As noted above, BnM does not trade in nor generate electricity, from gas, however we are at a loss to understand why the RAs are making this 'geographical' distinction in the Consultation paper. As a matter of fact, 'daily' products are available in NI, but as pointed out in the paper such products must be 'purchased' at least 12 days in advance; it would appear that this requirement for pre-purchase is the basis for the SEMC's distinction. Is this a valid reason for the segregation of the market? It must be remembered that units in RoI can purchase 'daily' products at any point from D-29 to day ahead (DA) gate closure. Referring to the text box in section 3.1 of the Consultation, the definition of the Short Run Marginal Cost (SRMC) is based upon the difference in costs between generating and not generating electricity 'during that day'. Logic then suggests that a 'daily' cost item, which clearly isn't a fixed cost, and irrespective of when it was purchased, is by definition a cost item which must be included in the SRMC under the principles of 'Cost Reflective' bidding. Bord na Móna contends that as there are 'daily' products available in both jurisdictions, there is no basis to segregate the market and that gas transport costs should be applicable for the SEM *in toto*.

Attributing a Value for Capacity

Bord na Móna appreciates there is a number of different ‘prices’ that, notwithstanding issues around transparency and liquidity, could conceivably be employed as a reference price to value ‘daily’ capacity. However, given the absence of a secondary market in NI, an opaque secondary market in RoI coupled to existing criteria in the BCoP (*where no recognised and generally accessible trading market exists in the relevant cost item the Opportunity Cost of that item should reflect the costs which would be incurred by the relevant generator in replacing that cost item*) an obvious and compliant method for attributing value for capacity already exists. This can be achieved by simply requiring participants bidding in gas fired units, to include in their bid the regulated price of ‘daily’ capacity, as this is by definition the *‘the costs which would be incurred by the relevant generator in replacing that cost item’*.

As queried in the Consultation paper, it can be concluded that there is no need for the SEM Committee to exercise its discretion to disapply the principles in paragraphs 8(i) and 8(ii) of the BCoP.

A decision to prescribe the bid cost of gas transport capacity as the regulated ‘daily’ price, complies with the existing code of practice. It is also aligned with an earlier SEMC decision¹ (again relating to the cost items in the BCoP) where the conclusions reached by the Committee were based on the objectives of *‘simplicity and transparency’* and also providing *‘regulatory certainty’*.

Risk associated with Choice of Capacity Products

Progressing from the logical construct in the above section, whereby participants with gas fired units are simply required to bid in the ‘daily’ regulated price, the complications outlined in the consultation paper, including *inter alia* which ‘price’ different generators bid and the increased burden on the Market Monitoring Unit (MMU), effectively evanesce.

Capacity Payments Mechanism

On its face, it is somewhat ambiguous to state in the Consultation that *“the cost of gas transportation has already been considered within the cost of a Best New Entrant when calculating the Annual Capacity Payment Sum[ACPS]”*. It is probably more accurate to conclude that the cost of gas transportation is a constituent variable considered when determining the model, fuel type(s) and location of the notional BNE peaker. Furthermore, the Consultation suggests that *“the inclusion of gas transportation capacity could be classified as a material change [emphasis added] to the SEM”* – this is simply not the case; the inclusion of the gas transportation as a SRMC cost item is aligned with the existing BCoP, there is no material change to the SEM. However, there may be a valid argument to re-assess the ACPS if the exclusion of gas transportation costs from ‘recurring charges’ in the determination of the BNE impacts on the model, fuel type(s) and location of the notional unit. Re-examining the data from the most recent BNE consultation in this manner (i.e. omitting gas transportation charges from the dual fuel units) does not alter the extant conclusion that the BNE peaker is a distillate fired plant in NI. In light of this conclusion, the recent SEMC decision² to *“bring some stability and certainty to the volatility in the capacity pot year on year”* by fixing and indexing the BNE methodology for 3 years (rather than recalculating

¹ SEM-11-055 “AS Arrangement and the BCOP Decision” at pp 6

² SEM-12-016 “CPM Medium Term Review – Final Decision Paper” at pp 13

annually) and the above mentioned fact that the inclusion of the transport cost of gas is not a material change to the SEM – there is no need to reopen the BNE process prior to 2016.

Methodology for Inclusion of Gas Transportation Costs with Commercial Offer Data

In the Consultation paper the proposed methods posited are dependent on a myriad of factors. Endorsing the conclusions outlined earlier in this submission eliminates the multiplicity of options and reduces the ‘methodology’ to a single, compliant outcome – all gas generators in the SEM to simply include the regulated market price for gas daily capacity in their COD.

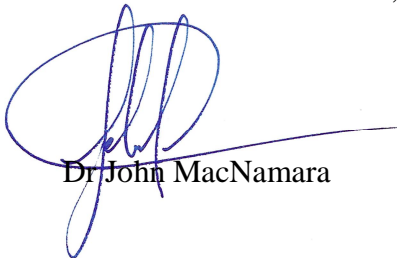
Summary

Although not yet a generator firing gas in the SEM, Bord na Móna believes that gas transportation costs, given the development of the gas markets on the island, are required under the BCOP to be included in the COD for all SEM participants bidding in gas units.

In the absence of a recognised and generally accessible trading market (both 1^o and 2^o) the ‘opportunity cost’ under the BCoP defaults to the replacement value of the daily product which in turn equates to the regulated price for gas capacity.

Existing data suggest that treating gas transportation costs as a fixed cost does not alter the model, fuel type and location of the 2013-2016 notional BNE unit.

For and on behalf of
Bord na Mona PowerGen,



Dr John MacNamara