Gaelectric Holdings Plc.

Response Paper to:

I-SEM Capacity Remuneration Mechanism Consultation Paper

SEM-15-044

Gaelectric Holdings Plc. Response

17/08/2015

Public

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1 CONSULTATION QUESTIONS

1.1 RESPONDENT DETAILS

COMPANY	Gaelectric Holdings Plc
CONTACT DETAILS	Brian Kennedy Senior Power Markets Analyst **Gaelectric Holdings Plc** Portview House Thorncastle St Ringsend Dublin 4 DD: +353 (0)1 643 0820 E: bkennedy@gaelectric.ie W: www.gaelectric.ie
MAIN INTEREST IN CONSULTATION	Developers and operators of renewable and energy storage projects, aiming to ensure that I-SEM CRM is designed in a manner which is equitable, and adequately considers new entrants and forms of renewable sources which provide capacity to the system.

1.2 GENERAL COMMENTS

Gaelectric Holdings Plc. ("Gaelectric") welcomes the opportunity to respond to the I-SEM consultation paper on the I-SEM Capacity Remuneration Mechanism. We welcome the effort of the SEM Committee (SEMC) in respect of the intense engagement currently ongoing in the I-SEM detailed design work stream, which has been particularly helpful for both decision makers and participants alike in understanding the concepts and subsequent issues relating to the I-SEM design.

Gaelectric is an independent wind, energy storage, solar and biomass developer operating within the Republic of Ireland, Northern Ireland, United Kingdom and North America. To date Gaelectric holds 150MW of generating assets across 6 projects in Northern Ireland and the Republic of Ireland, and a further 40MW of 'shovel ready' projects with grid connections and full planning approvals in place.

Gaelectric's near term pipeline on the island of Ireland is circa 320MW with the expectation that the company will have 400MW of projects generating power by the end of 2017. Furthermore, Gaelectric has acquired Imperative Energy Ltd., a leading supplier of bioenergy solutions to a number of sectors throughout the UK and Ireland.

Having developed our portfolio of wind assets through early stage planning into construction and operation phases, and in doing so becoming one of the largest independent developers on wind energy on the island, Gaelectric are acutely aware of the challenges that are faced by renewables on the island as a result of the development of the I-SEM. Specifically, we are cognisant of the increased risk on wind posed by the proposed I-SEM design and the Reliability Options (RO) in particular. We are nonetheless supportive of the I-SEM programme provided it adequately considers the very specific technical capabilities of intermittent renewables.

Gaelectric have made representations regarding the need to include renewable technologies in the RO, including wind technologies that are in receipt of renewable support mechanisms. It is our contention that the CRM as designed places an emphasis on delivery and a risk on non-delivery and is therefore not considered a subsidy, but rather a contract for service. Given this, and the fact that the all-island market does not feature renewable support measures such as the carbon price floor; we believe that all intermittent renewables (including those included in a government support scheme) should be eligible for CRM contracts. These projects should be supported further by allowing portfolio bids which allows thems to compete on a level playing field and moreover protects investments which have been made or are being progressed on the basis of revenues from the capacity mechanism. We request early certainty in this regard given the impact that the ongoing uncertainty is having on planned investments.

In addition to our extensive wind portfolio, Gaelectric and Tesla have announced the purchase and planned deployment of Tesla Energy's first battery power utility-scale project in Ireland. Tesla and Gaelectric will work together to develop a pipeline of battery projects. Initially we expect a 1 MW demonstration to be developed, targeted for deployment in 2016. Given this and the development of Project CAES in Northern Ireland, which has an agreed connection offer in place with SONI, we have considerable interest in the development of a capacity remuneration mechanism which incentivises new entrants, and promotes an exit signal for capacity providers who are uneconomical.

In respect of these projects, we support entry signals for new technologies such as storage which are recognised as being vital component of the diversifying energy mix which is a feature of the all-island market. We support the proposal in section 4.10.2 of the consultation which indicates that aggregators can bid portfolios into the RO auctions, and particularly the concept of aggregating storage assets in this manner also. This will support the operation of storage on a level playing field in the RO.

Furthermore in relation to energy storage, Gaelectric strongly advocate a position which does not charge energy storage an RO fee, given that the technology does not have the right to self-commit and would therefore never be dispatched on during a stress event. Moreover, if storage is obliged to pay an RO fee on the demand portion, it would then need to be included in the LOLE calculation. The result of this is a need to contract with increased generation and a corresponding increase in the costs to consumers.

Gaelectric request that further clarity is provided to the objective of the RO, i.e. is it the objective to ensure long term security of supply? Or is the design borne of a need to mitigate high prices in the short term to protect consumers> We believe that these are mutually exclusive options, and request that adequate emphasis is placed on securing the long term interests of the consumer. We do not believe that an RO which serves the sole desire of managing short term costs to consumer will address long term price stability. It is clear that new entrants rely on the SEMC taking a longer term view of the RO objectives.

Given our comments above, we believe there is an acute need to ensure that the RO design encourages market entry for new entrants which are both flexible and reliable, and which will support the increased integration of renewables on the system in a secure manner. This will ultimately serve the best interests of the consumer over the long term. Our response intends to address these challenges and provides options on how best to support market entry.

2 SUMMARY OF RESPONSE

A summary of the key points within this response are outlined below;

- The Reliability Option should be focused on securing the long term security of supply on the island and new entrants should therefore be actively incentivised.
- New entrants require a minimum of 15 year capacity contracts.
- Renewable Energy sources in receipt of a support should be eligible in the RO.
- Penalties for technologies (aside from intermittent renewables) should be subject to explicit delivery incentives.
    - An exit signal should be designed in for uneconomical plants, and corresponding new entrant entry signal needs to be incentivised.
- Intermittent renewable technologies should not be exposed to explicit incentives given this cannot incentivise them to alter their behaviour as their primary fuel is outside of their control.
- The practical interaction between the RO and DS3 for new entrants is crucial, adequate consideration needs to be given of this.
- New entrant commercial terms should be grandfathered to provide investment certainty. The long term contract should not have automatic review periods.
- Scarcity Pricing is more appropriately dealt with in the Energy Trading Arrangements work stream.
- The Balancing Market should be considered further in regard to the Reference Market, whilst we have queries as to how the Split Price Market option works in practice.

2.1 Capacity Requirement

The SEM Committee has requested feedback on this section, including;

A. ***Feedback on our minded to position to retain the all-island security standard of 8 hours LoLE.***

Gaelectric do not agree with the analysis which places an emphasis on the costs of reducing a security standard of 8 hours without equivalent examination of the benefits associated with such a move. Furthermore in the context of the value of the entire capacity market, the quoted costs for moving LOLE to a level of 3 hours is relatively low at up to €19.1 million/year (gross of any benefits).

In operation, we understand that the TSOs operate to a tighter standard than the 8 hours indicated in the paper. Furthermore, infrastructural inadequacies currently permeate through to a non-uniform standard on the island. In taking the opportunity to develop an all island scenario, we see no reason why the I-SEM should not be in line with our European neighbours, particularly in the France, UK, Ireland (FUI) region, and consumers should be as well protected as their European counterparts.

Given the above, Gaelectric favour moving to 3 hours.

In respect of the review guidelines, Gaelectric support that the security standard should be assessed every two years as per ENTSO-E requirements, however any review should have no impact on long term contracts already agreed.

B. ***Comments from respondents as to their preferred method of accounting for the unreliability of capacity in determining the capacity requirement, along with reasons behind their preference.***

We do not necessarily agree that the Total Requirement method would be distorted in favour of unreliable plant, provided the delivery performance signals (i.e. performance incentives) were strong enough to promote reliable plant and to create an exit signal for unreliable capacity providers.

Gaelectric have concerns as to the methodology for de-rating capacity in the "De-Rated Requirement" option given it is unclear as to how the de-rating would be decided. This is particularly an issue for new entrants/new technologies where the TSO has no prior experience with the technology on the system.

Gaelectric support the "De-Rated Requirement" option, however we encourage full consultation and transparency over the methodology for de-rating.

C. ***Feedback on the options presented in relation to accounting for demand forecast uncertainty, along with rational behind any position.***

Gaelectric do not agree with the use of a Single Average Scenario given it will not consider an adequate range of scenarios. It is also at greater risk of producing an inaccurate demand forecast should their not be a robust set of assumption made in coming up with the single scenario.

It seems that the "Optimal Scenario" option will indicate the most reasonable approach which is well considered. Notwithstanding this, further information should be published on this proposal, perhaps using an example.

D. Feedback on our minded to position to base the capacity requirement for the CRM on a single capacity zone.

Gaelectric prefer to concentrate here on the need for capacity in each jurisdiction rather than the zoning of the auction. It is clear that there is a distinct need for long term capacity in Northern Ireland and therefore a locational signal is absolutely required within the competition. We strongly support a design which considers the *need* for capacity in both zones separately. Whether this capacity is realised in the same auction or a dual zone auction is then a matter of detailed design. The design of the auction must consider the need for new entrants alongside the DS3 procurement mechanism and the SEMC should ensure that the capacity market does not block new entrants that would otherwise have commissioned owing to positive DS3 signals.

We therefore strongly contend that the RO should be designed with a view to maintaining long term security of supply which is in the interest of consumers and supports achieving government policies on decarbonisation and further to achieving renewable objectives. In consideration of this, we encourage the SEMC to ensure that both jurisdictions ensure that there is a clear path for new entrants, and indeed targeting a new entrant in both jurisdictions should be a key objective of the initial auctions.

The query regarding a single or dual zone relates somewhat to the need for infrastructure development, i.e. the acute need to develop the North-South Interconnector as a key piece of enabling infrastructure. Gaelectric support the expedited delivery of the North-South Interconnector however notwithstanding this, we disagree with the degree of reliance on the North-South Interconnector to support security of supply in Northern Ireland, and therefore contend that new entrant technologies are vital for both jurisdictions to maintain long term security of supply. Additionally, there is a very clear risk to the timely implementation of the North South Interconnector, and as such the design should be considered as satisfying security requirements absent this piece of infrastructure.

The mere introduction of a proposal for multiple zones seems to reflect an acknowledgement of the need for both jurisdictions to ensure that new and existing capacity clears the auction.

Gaelectric promote early consideration of security of supply within this consultation.

The proposal; "Locational Price Adjustment" is unclear, however the option seems to suggest that the cost of network reinforcements when choosing one capacity provider over another will be backed off the bid of the successful party. This is overly complicated, does not lend to investment certainty and the likelihood of challenges by participants will be high. We therefore do not support further consideration of this proposal.

2.2 Product Design

It is important that the product design reflects the objectives of the RO work stream. Gaelectric favour transparent processes which are easily understood to lending institutions such that risks can be adequately assessed. Furthermore we believe that the RO should act as a strong delivery/reliability incentive to all generators awarded a contract. If adequately designed this will create an exit signal to uneconomic generators and a corresponding entry signal for flexible and reliable new entrants.

The need for an investment signal is being addressed through the DS3 work stream to the extent that 15 year contracts are being proposed with 20 year take or pay contracts being awarded on a case by case basis. The DS3 work stream is however only one element of the investment case for new entrant technologies which is equally supported by a need for signals emanating from the energy and capacity market.

Gaelectric request that the SEMC give the requisite attention to the need for new entrants to address renewable integration challenges, security of supply, and not least the critical need for greater flexibility in the Energy Trading Arrangements. The design of the RO will heavily influence this investment signal, specifically the performance incentives and reference pricing.

We believe it is critical that windfarms (operational and future facilities) are eligible for the RO market, and the design of the product itself needs to reflect the links to the Northern Ireland EMR CfD programme (reference market), potential REFIT reference markets, and importantly should not penalise the intermittency of the technology on the understanding that intermittent technologies do not have control over their fuel source, and as such cannot modify their behaviour to adapt in light of performance incentives.

The SEM Committee has requested feedback on this section, including;

A. ***The approach to setting the Reliability Option Strike Price;***
    a. ***Should we adopt the "floating" Strike Price approach, which is indexed to the spot oil or gas price?***

Gaelectric favour the floating strike price option.

From the perspective of new entrants, we support grandfathering of the reference unit and the strike price. To do otherwise will introduce considerable risk premiums being built into new entrant bids given the uncertainty in the value of the RO to the facility over the life of the contract.

It is clear that long term contracts are a necessity of financing a large scale energy asset, and 15 year contracts for capacity, in parallel to other initiatives supporting new entrants, will improve the commercial viability of these assets. However where risk such as movement in the reference unit/strike price is introduced into the contract, a new entrant's benefit of the long term contract is vastly eroded given the need to mitigate the risk by introducing risk premium pricing in the bid.

We request that the SEMC recognise the value of new entrants and the benefit they can bring to the system in terms of flexibility. Moreover new entrants require recognition that their risk profile is not equivalent to that of incumbent generation and no grandfathering will act as a barrier to market entry.

b. ***How do we choose the reference unit? Should it be based on the actual plant on the system or a hypothetical best new entrant (BNE) peaking unit as currently used for setting the Annual Capacity Payment Sum?***

Given the need to ensure that the Best New Entrant will be in a position to actually contribute to the RO, a margin above its cost will be required, rendering the Best New Entrant plant more akin to a hypothetical option in any case. Gaelectric support the premise that the Best New Entrant (+ margin to ensure best new entrant can contribute) will continue to be the reference unit on the island, given this methodology retains an element of continuity with the existing approach. The Best New Entrant method will also act to ensure that there is transparency in the process of choosing the reference unit.

c. ***Should we grandfather this reference unit where a multi-year RO is sold***

As indicated above, new entrant technologies require a higher degree of certainty than incumbent generation. This position is supported by the SEMC decision to propose 15 year contracts to new entrants within the DS3 programme (20 year contracts to be awarded on a case by case basis), and the indication here of long term contracts up to 15 year in tenor. However the certainty achieved by these contracts is not determined solely by the tenor of contract, but also the security of terms within that contract. Gaelectric are confident that adequate security can be achieved whilst retaining sufficient competitive tension in bidding to ensure value to the consumer over the period of contract.

With this in mind, Gaelectric are strongly supportive of a grandfathered reference unit for multi-year RO contracts, and indeed we believe this to be a pre-requisite for new entrants to be in a position to consider investing to the point of qualification for a competition. We have called for contracts of up to 15 years for new entrants to be introduced and were the reference unit reviewed on a regular basis, a long term contract could be reviewed numerous times in its lifetime.

Any review of commercial terms within the lifetime of the contract will render the effective banking period only as long in tenor as the period from commencement of the contract until the first review.

Our assessment is that without a grandfathered approach, bidding for multi-year contracts could become uneconomical given the uncertainty of risk in the latter years of the contract, and hence the increased risk premium which would be required in the initial bid. The resulting bid formats would be particularly volatile as each operator will have a varying perception of the risk to the facility.

Indeed, even with an increased risk premium, we understand that lending institutions would not be comfortable with the risk imposed on the project and would therefore withhold lending to the project.

d. ***The implementation of scarcity pricing in the I-SEM Balancing Market?***

Gaelectric are generally supportive of the need to ensure balance responsibility is incentivised in the energy trading arrangements and also to incentivise reliability of delivery in the CRM.

Scarcity pricing serves two purposes; in the short term it sends a signal for the market to balance itself where a shortage occurs or where a voltage reduction has occurred, indicating the need for capacity. In the medium to longer term, its purpose is to compliment a capacity mechanism in facilitating market entry of new resources and on the corollary to signal the exit of resources which are no longer economical nor reliable. In this regard, Gaelectric support measures to incentivise market entry and reliable and responsible operations.

However, notwithstanding our position above, it is clear that the implementation of scarcity pricing in the I-SEM will have farther reaching impacts than just the RO, and as such this should be considered separate of the CRM work stream, and perhaps more appropriately in the Energy Trading Arrangements work stream.

e. ***The choice of market reference price options from amongst the options presented and consistency with key objectives.***

As a precursor to our response here, we wish to highlight that there is a clear relationship between the reference market and other ongoing work streams such as the review of REFIT and the EMR CfD programme. Any decisions taken here must reflect due consideration of the direction of these work streams. In addition to this, the impact from DS3 should be adequately considered also.

In regard to the key factors driving the choice of the Market Reference Price, there is an obvious conflict in the considerations put forward in the paper. For example, optimisation of IC trading and incentivising availability at times of system stress are two factors which are best served by differing markets. IC trading will be focused on the DAM where I-SEM is coupled with other European markets, and system stress is most likely to present itself in the balancing market as opposed to the DAM.

The introduction of scarcity pricing may address these issues given a DAM reference market and scarcity pricing in the balancing market, however as discussed above we believe that scarcity pricing is an issue to be addressed in the Energy Trading Arrangements.

Nonetheless we believe that further clarity should be provided on how these criteria are to be weighted.

Intra-day Option

It is apparent that the Intra-Day Market would be an inappropriate market place given there is no clear market price and therefore transparency issues arise in addition to issues regarding the signal for delivery. In the IDM it would not be clear that a delivery signal has occurred if the clearing price they have received for their energy is considerably lower than that of the marginal unit. This is by no means a trivial issue given the lack of liquidity that could be expected in this market.

Day Ahead Price Option

Owing to a lack of scarcity in the DAM caused by the fact that unplanned outages are highly unlikely to present themselves in this market means that the incentive to deliver here is considerably reduced.

As a result of this, the capacity market is unlikely to incentivise delivery or reliability of capacity providers.

As previously outlined, Gaelectric favour a market designed in a manner which incentivises economical plants to stay online, however which would signal the exit (from the CRM at least) of uneconomical plants. This will not be achieved by a DA reference market.

The DAM does however have advantages, particularly in regard to the ability of participants to hedge their positions.

Blended Price Option

Equally, we do not believe there is merit in further consideration of option 4a (Blended Price Option) given that the strike price will not change depending on the market traded which will counteract the delivery signal by allowing capacity providers to negate the signal in one market by trading in another.

Split Market Price Option

Option 4b represents an improvement on option 4a, however it seems particularly complex and it remains to be understood how it would be implemented. There is no discussion in the Split Market Price Option as to how the strike prices would be devised. For example, would there be two strike prices or a single strike price? Without this information, it is not possible to indicate a preference for this option.

Balancing Market Price Option

In respect of a Balancing Mechanism reference market with a mandatory/incentivised DA offer and virtual bid, Gaelectric view this as being worthy of further consideration given it will accurately value scarcity whilst ensuring DA liquidity is not sacrificed by virtue of the buy back.

Gaelectric would support further consideration of this option, however it is clear that further information is required to be published ahead of making a decision.

Furthermore, we do not believe however that this decision can be made in absence of further information of the treatment of support schemes in the market given the clear relationship between these. A clear timeline should be provided to industry as to how the SEMC intend to liaise with the DCENR and DETI on the respective reviews of subsidy schemes, and their impact on this work stream.

f. ***Whether the RO volume and/or the additional performance incentives should be load-following.***

Gaelectric support the concept of load following which will reduce the obligation in the summer months when the need for service is not as acute.

We do not however support any proposals to scale up the requirement of a plant on the basis that the SO has under-forecasted its demand. If this risk is to be covered off by the TSO, we suggest that a factor of safety is built into their estimates of contracted capacity providers.

g. ***The requirement for, and design of additional performance incentives, including;***

Gaelectric do not support the ongoing use of the BCOP given its clear restrictions under a market such as the I-SEM. We believe that regulatory constraints should not be permitted in the market where they can impact the incentivisation of plants to operate.

We support the introduction of performance incentives for plants to ensure a strong delivery signal for plants on the system. For conventional generation contracts we do not necessarily agree with the limitation of penalties to such that there is no strong incentive to ensure reliability over the course of a contract year. In GB and ISO-NE, penalties are capped over the course of a year at 100% of the revenue which could be earned.

In GB, it is clear that the design of the capacity mechanism resulted in the the opportunity for large scale new entrants becoming particularly limited.

It is our contention that the scheme in GB extended the life of coal plants on the system, and incentivised the introduction of unreliable plant into the mechanism for the reason that these plants were at no loss for not contracting for capacity.

As a result, the clearing price of £19.40/kW results in one large scale new entrant (Trafford CCGT) which resulted in a low cost to consumers (circa £11/household). The auction resulted in no exit signal and therefore no corresponding entry signal for new capacity. What is clear is that this auction has done very little to enhance Britain's long term security of supply, and whilst the near term concerns are somewhat offset, the fundamental issue of achieving long term security of supply in a manner which also promotes wider objectives of addressing the need flexibility and efficiency targets, has not been addressed.

We therefore request detailed consideration of the objectives of the RO, and further consultation on how the RO will be designed with a view to securing the long term interests of the consumer. This would include a review of the lessons learnt in the GB proposed mechanism and how an alternative incentive regime could signal the appropriate entry/exit signal.

In respect of the appropriateness of incentives on all technologies, this is clearly not a valid argument. Incentives for delivery are introduced to ensure that capacity providers actively manage and tailor their behaviour in a manner conducive to the RO objectives. It is expected therefore that the introduction of incentives will ensure that capacity providers tailor their behaviour to avoid charges and penalties.

Intermittent renewable technologies however are not in a position to tailor or modify their behaviour, even as a result of the existence of incentives. The fact remains that the fuel source for the likes of wind energy is intermittent, and therefore these projects operate at the behest of their fuel, i.e. the weather.

Therefore, to impose penalties on a capacity provider who had no tangible opportunity to manage their behaviour would be wholly inappropriate.

Instead, Gaelectric propose the following to allow intermittent renewables to compete on a level playing field;

- Renewables to be exposed to difference payments capped at 100% of annual revenue.
- Renewables would not be exposed to explicit penalties
- Renewables would bid as an aggregator, irrespective of the size of the project within the portfolio (i.e. no limit on the size of a windfarm that can enter a portfolio).

We believe these 3 key components will provide intermittent renewables with a fair opportunity to trade in the RO in a manner which creates an acceptable risk profile.

a. ***The form of additional incentives;***

Gaelectric support the introduction of over delivery payments and under delivery penalties for conventional capacity providers, however as outlined above we do not believe intermittent renewables should be exposed to explicit penalties for non-delivery. This has the effect of locking wind out of over delivery payments also.

Given that contracted plants will likely be de-rated but will equally likely have the uncontracted capacity available to them in a stress event, we support the prospect of over delivery payments for this capacity. The same principles follow in the instance where load following obligations are introduced. If there is an over delivery by a generator unit, it should be paid for that.

We anticipate that over delivery payments are likely to be funded from a pot formed from under delivery penalties. We request further feedback on this.

As indicated above, Gaelectric are keen to see an adequate reliability signal develop in the RO and we request that the charging methodology for penalties and payment for over delivery should be further consulted upon.

b. ***Scarcity based triggers for performance incentives***

Gaelectric do not believe that there is sufficient information presented in the document to take a position on this.

c. ***Caps and floors on incentives;***

Gaelectric's position, as outlined above is not to expose generators to uncapped losses in the RO, but to develop a reasonable approach which creates an exit signal for generators who are uneconomical and unreliable. We believe there should be some element of a cap on incentives which can be taken into consideration for bidding purposes, however we disagree with the penalty regime that was implemented in the GB capacity mechanism. In GB, it is clear that the penalty caps results in a number

of inefficient and unreliable plant entering into and clearing the competition in the knowledge that over the course of a delivery year there would be no total risk on price for extreme non-delivery.

As a result there was a lack of an exit signal presented to the market and there was an obvious lack of new entrants in the cleared auction.

The same rules apply for New England which will create a cash flow issue for continuous non delivery over the course of 1 month, however utilities are aware that at worst they will remain even for the year and will not be subjected to a total loss. It is understood that the cash flow issue presented will create a risk for incumbent generation, however this has not proven to be a risk that impacts on the viability of providers in similar markets.

The economics of the plant is then largely irrelevant, and as such this prevents exit signals and similarly acts as a barrier to new entrants.

We contend that the decision to be made here speaks to the ambition of the SEMC to realise new entrant technologies on the system, and we request due consideration of this in the detailed design process.

d. ***Performance incentives for renewables and DSUs;***

We refer to our response in the above questions in regard to the treatment of renewables. Specifically, the maximum penalty should represent a liability for a capacity provider over the course of a year, which encourages delivery signals and reliability. We do not believe that the GB proposals achieve this.

It is clear that intermittent renewables are and should be viewed differently given they have no control over their fuel source with which to modify their behaviour. There is therefore no obvious benefit to apply incentives to intermittent renewable generators, in the same manner as conventional capacity providers who can modify their strategy to ensure reliable delivery.

We therefore support the inclusion of wind against the backdrop of the risk of difference payments (capped at 100% of total revenue for intermittent technologies) however we do not support explicit incentives for wind. In taking on the risk of difference payments alone, wind generators will face a risk and would therefore need to carefully consider their inclusion in the competition.

Portfolio bidding should be introduced for wind and indeed storage to manage the risk of difference payments.

e. ***Performance incentives during the pre-commissioning phase;***

We support milestone delivery plans backed against construction bonds for new entrants which will serve to disincentivise “cardboard generators” who can bid on a speculative basis, blocking legitimate new entrants.

f. ***Detail of any other considerations respondents feel that we should take account of when determining policy in relation to product design.***

In addition to portfolio bidding for wind, Gaelectric support the indication in par 4.10.2 that energy storage could be accepted in a portfolio. We believe that energy storage will provide a very valuable resource in terms of capacity provision to the system, both on a bulk scale and through decentralised developments, and we fully support any provisions which allow the aggregation of these technologies.

We request that there is a detailed consideration of secondary trading markets given the need for generators to hedge risk on outages etc. The existence of a secondary market will have a material impact on the structure of bids into the primary market given the opportunity for risks to be better managed.

2.3 Eligibility

As a precursor to the response to this section, Gaelectric wish to highlight the need for consideration of the DS3 programme and the synergies between both the RO design and the DS3 design.

We consider in our response the need to account for the outcome of the DS3 competition for new entrants before construction/performance bonds become live. Gaelectric have previously raised concern as to how both programmes will be managed in parallel given the need for a new entrant to potentially clear both auctions before its business plan being satisfied.

With this in mind, we propose that the SEMC give consideration to combining the auctions/ elements of the auction, at least for new entrant technologies. The benefits of doing this would include;

- More understandable risks for lending institutions/investors
- Reduction in the cost of competition
- One credit cover provision as opposed to two
- More certainty to new entrants and investors
- Bids can be made conditional on one another clearing.

We believe this would have a material impact on the competitiveness for new entrants,

The SEM Committee has requested feedback on this section, including;

A. ***The options presented in relation to the eligibility of plant supported through other mechanisms.***

Gaelectric strongly support Option 3 which keeps the CRM open to all technologies and all renewable projects.

It is important to note that decisions here will have a considerable impact on the renewable industry and the investment climate for renewables in both Northern Ireland and the Republic of Ireland. Business plans and investments have been, and continue to be made on the basis of the inclusion of capacity revenue streams for wind projects throughout the island and to remove this completely would be an unacceptable retrospective change for the renewables industry. Furthermore, this would do considerable damage to the view of the island of Ireland as a favourable place to do business in the renewable industry.

From the perspective of REFIT projects, we view this as a cost neutral approach given that the PSO will inevitably top up the generator in any case and consumers will pay for both the PSO and the RO. However we believe it would be inappropriate to lean on the PSO directly to top up wind farms given the impact this will have at consumer level and also in regard to the cash flows on wind farms and the corresponding effect on the pricing of PPAs to manage this cash flow risk.

Regarding ROC projects in Northern Ireland who are particularly at risk here, there is no avenue available for these generators (in operation and significantly developed) to recoup the lost capacity revenue should they be excluded from consideration on the RO. This is a particular risk for Northern Ireland participants and to investments made in Northern Ireland renewables to date. We note the

current uncertainty regarding renewables in Northern Ireland and request that the position regarding renewables within the RO is addressed in an expedited manner to limit the impact on investment.

An important point to note is that in GB, whilst plants in receipt of renewable subsidies were not considered eligible for the capacity mechanism, the GB government have a strong renewables market enabler in the carbon price floor which does not exist on the island of Ireland to support renewable policy. We therefore believe that this revenue stream should remain open to all forms of renewables, including those in receipt of a renewable support.

Ancillary Services

For clarity, Gaelectric do not believe that contracts for ancillary services (DS3) and RO represent a double payment in any way. There should therefore be no limitation on these contracts.

We note that many new entrants will need surety over both the RO and DS3 auction results before committing to build. This needs to be built into the design process.

Non-Firm Generation

It is apparent that non-firm generation retain a higher risk in the RO than firm generation. We do not however believe that this should impact on the de-rating factor given that the operator will be able to make a decision as to the ability of that plant to manage the enhanced risk, and will therefore manage their bids accordingly. We do not support the further erosion of volumes eligible for contract and instead believe that the performance incentive regime that we have supported will ensure that all operators of non-firm generation will themselves "de-rate" their capacity to the appropriate level to ensure all risks are managed effectively.

B. ***The options for eligibility of demand side and storage providers.***

Gaelectric welcome the consideration of energy storage in the context of the RO. Gaelectric believe that all types of energy storage should be considered eligible for the RO as per the EEAG principles.

Some energy storage technologies will be developed with smaller storage mediums in mind given their need for faster acting performance. We do not believe this should limit their participation in the RO and furthermore we support the inclusion of energy storage technologies in a portfolio bid which acts to aggregate these technologies and hence better equip the system to manage with system stress events. We believe the analysis considered in par 4.8.3 is incomplete and does not consider the secondary trading opportunities or portfolio bids which should exist for energy limited plant.

We have considered the design of the RO and do not believe that it would be appropriate to charge the demand portion of energy storage an RO fee as this would result in a need to consider this demand as part of the LOLE calculation and hence contract for this volume on the generation side also, raising cost to consumers.

This position is reinforced by the fact that storage is not self-committing and would therefore not be in a position where the demand side is operational during a stress event. The demand element of

storage does not therefore contribute to stress events and it follows that no RO fee should be payable on this volume.

C. ***Do you have a view on the technology vs plant specific approaches to de-rating?***

It is not made entirely clear in the paper how the de-rating figures will be arrived at in either option, and therefore we would require to see further proposals on the methodology to take a view. We recognise that it is likely that the de-rating factors will be similar whether applied on a case by case basis or per technology class in any case.

The SEMC should give consideration on how to treat new entrant technologies and whether these will be consumed within a technology banding (for example CAES within the Storage banding), or treated on a case by case basis.

Intermittent renewables should be contracted up to their average capacity factor across the board. Gaelectric have previously stated that we believe that intermittent sources of energy should be permitted to be grouped together and bid as aggregators. We believe this will mitigate the inherent risk to intermittent technologies in terms of ensuring delivery. We support consideration of cross technology aggregation within intermittent technologies.

D. ***Do you have a view on the historic, projection or hybrid approaches to de-rating?***

Historical data or the hybrid approach seems the most reasonable for this. In the hybrid approach, we request feedback on what projections/scenarios would be permitted in calculating the figures going forward.

E. ***Do you have a view on grandfathering of de-rating factors?***

Under our proposed approach outlined above, we do not believe grandfathering is appropriate for any technology on a short term contract and as such we support a pro-rata approach.

For clarity, we oppose any changes to the de-rating factor for power plants bidding in for a 15 year contract should have their de-rating factor eroded during the period of the contract.

F. ***Do you have a view on options presented with respect to the non-firm generation?***

As previously indicated, we believe non-firm generation should be allowed to enter the competition with the risk of non-delivery within their control rather than have a further de-rating factor applied to the non-firm portion of their capacity. Given the proposals on delivery incentives that we have put forward, we believe there is adequate incentive for non-firm capacity to effectively de-rate itself to an acceptable level to manage its risk.

Para 4.5.4 states that if some non-firm capacity is cheap enough it should have access. Given it is proposed that contracts should be awarded on a non-discriminatory basis via a procurement exercise, we reject the assertion that cheap non-firm generation could be awarded contracts whilst generation which isn't cheaper should be excluded. This is a subjective approach not befitting the proposals in the HLD.

Gaelectric therefore support the design of option 1; Eligible to bid, subject to same de-rating factors.

G. ***What evidence should an aggregator be required to show physical backing?***

A letter from the Generator and the aggregator outlining that both are subject to a contract should suffice in this regard. We do not believe that using a PPA as evidence is an onerous requirement on aggregators.

H. ***Should there be a maximum size of unit that can bid into the RO auction via an aggregator, and if so what is the threshold?***

Gaelectric do not support the limiting of a unit size within an aggregator. It is clear that some operators of large scale renewables/storage will not be in a position to bid in their projects and will require a PPA provider to aggregate the portfolio. By making some projects compete outside of an aggregation service by virtue of an arbitrary limit imposed on eligibility criteria would unduly negatively impact the competitiveness of the project in question.

There may however need to be consideration of a maximum size of aggregator depending on the assessments of this in the market power work stream.

I. ***Should there be a minimum size below which a capacity provider may not bid directly into the RO auction, and must bid via an aggregator? If do what is that threshold?***

Gaelectric do not see any reason why a minimum size should be prescribed so long as the projects in question are adequately metered within the aggregator.

J. ***What pre-qualification criteria should be applied?***

Gaelectric support the introduction of pre-qualification criteria which will ensure that all potential capacity providers are sufficiently capable of delivering capacity as per the requirements of the design of the RO.

For new entrants, whilst we support the use of construction performance bonds, we remind the SEMC that new entrants will also place a reliance on the DS3 auction results before committing to their build programme. We believe the SEMC needs to give further consideration within the DS3 and I-SEM work stream and how the competitions interact with one another.

We support the requirement to use an adequate level of project permission in pre-qualification which indicates both the substantial development of the project and the commitment of the sponsors to the project in question.

The question that arises here is the various level of consents and permissions which applies to projects including conventional technology, onshore wind and Compressed Air Energy Storage and Offshore wind which demonstrate a significant commitment by the project sponsor.

Gaelectric support the idea that planning permission would be used as the adequate level of consent/permission for projects to progress in pre-qualification *with the exception* that we believe the previous decisions relevant to adequate consents should be respected in all cases.

Specifically the decision of SONI/NIE in the Generator Connection Decision Paper (22 July 2013)[1] as endorsed by the SEMC (25 June 2013)[2] stated the following;

"As this is a unique situation SONI and NIE feel that it is reasonable for CAES [Compressed Air Energy Storage) to apply for Grid Connection as the Mineral Prospecting Licence provides the required level of assurance that the project will proceed. SONI will therefore accept a Connection Application from Gaelectric"

It is generally agreed that the use of planning permission is to "test" the commitment of a developer to the project in question, and indeed to ensure there is no hoarding of capacity or "bed-blocking". The fact is that Project CAES Larne NI is a project which requires a number of consents and there is no single test of commitment (CAES requires planning permission for the CAES station and marine licence {which requires full assessment similar to planning applications} separately), unlike other conventional projects. It is our view, as supported previously by the SEMC that an adequately strong test of commitment to the project is the Mineral Prospecting Licence which is awarded by the Department of Enterprise, Trade and Investment for Northern Ireland.

The Mineral Prospecting Licence provides for a considerable degree of commitment and both legal and statutory obligations on Gaelectric Energy Storage Ltd to develop and progress the project. The licence is time limited and therefore mitigates a hoarding of capacity, and Gaelectric commit to schedules of work and spend in order to maintain the licence.

Gaelectric believe that the same criteria should now be applied to the I-SEM competition qualification criteria.

We welcome discussion with the SEMC regarding qualification criteria for new entrants.

In addition to the above consent requirements, an accepted grid connection offer (received by the System Operator) should be presented for qualification purposes.

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1 http://www.soni.ltd.uk/media/documents/Consultations/Generator%20Connection%20Process%20Decision%20Paper%20-%20July%202013.pdf

2 http://www.allislandproject.org/en/transmission_decision_documents.aspx?article=a4ea3042-4dc6-4018-a6cc-cee152ade157

Gaelectric further support the use of a Construction milestone plan as evidence of the timeline in the qualification phase. We emphasise the need to consider the DS3 auction and the results of that competition before the construction milestone plan for new entrants is binding.

In regard to land control, we support the need for a director's certificate confirming ownership, lease or an agreement to lease land to be in place for the project in question.

In respect of the Business Plan which is proposed in table 4-4, whilst we support a board-approved business plan, the qualification stage will occur in advance of financial close for new entrants and as such it is too early to secure contracts for key infrastructure. Nonetheless the business plan should show a project ready to close out such agreements, and as such sufficient progress will need to be presented within the business plan.

Regarding credit-worthiness, Gaelectric support consideration of this, however specific details of this should be consulted on. We emphasise the need to work with new entrants on forming these proposals also. Gaelectric welcome engagement with the SEMC on this area.

K. ***Detail of any other considerations respondents feel that we should take account of when determining policy in relation to eligibility?***

As outlined above, Gaelectric believe that earlier decisions relating to the adequate level of permission for projects should be respected. We specifically emphasise the decision by NIE/SONI in July 2013 to accept Project CAES NI entry into the ITC with a Mineral Prospecting Licence acting as the required level of permission/consent for the project.

2.4 Supplier Arrangements

The SEM Committee has requested feedback on this section, including;

A. ***Whether the recovery of CRM option fees from Suppliers should be on a flat, profiled, or focused basis.***

Gaelectric have a preference for a focused basis.

B. ***Whether the Supplier credit cover arrangements for the I-SEM CRM should be broadly similar to those under the SEM, and whether / what credit cover arrangement should be introduced for capacity providers.***

Gaelectric believe the credit cover arrangements should generally be minimal and would require consultation on the methodology used to calculate the quantum of credit to be lodged.

We believe that where the credit cover is not adequate in a default event, future payments can be withheld from the defaulting party.

The SEMC should be cognisant of the impact of this on new entrants. Increased costs providing to new entrants for providing for credit cover facilities will be reflected in the bid for new entrants. Given the risk is generally quite low, we favour the alternative approach set out above.

C. ***Whether the costs of exchange rate variations (arising from the differences in the €/£ exchange rate at the time capacity is procured and its subsequent delivery) should be borne by capacity providers or mutualised across the market.***

Gaelectric believe this costs needs to be borne by the market rather than on capacity providers.

2.5 Institutional Framework

The SEM Committee has requested feedback on this section, including;

A. ***Are the above outlined governance arrangements suitable for implementation of the I-SEM capacity mechanism?***

Gaelectric share concerns regarding the implementation of the governance arrangements, particularly in respect to the relationship between EirGrid's contracting body and the East West Interconnector. We believe there is a conflict here which must be addressed by EirGrid.

We await further design information before making comment on potential remedies.

B. ***Which options for contractual arrangements are the most appropriate as assessed against the listed criteria?***

We prefer the Separate Option Model given that it clearly defines a contract between the capacity provider and the generator company. This will be a minimum and absolute requirement during an investment due diligence process. It is not clear that the same can be said of the Rules Based Model.

C. ***Are implementation agreements required for new entrants participating in the capacity auctions?***

Gaelectric support the use of implementation agreements for new entrants which will ensure that the projects entering into the competition in the first instance are viable.

We remind the SEMC that the implementation agreement will be dependent on a new entrant also achieving adequate results in the DS3 procurement exercise.

Given the importance of the detailed design on the Gaelectric Group and its assets in developing a significant cross technology portfolio within the timeframe of this market redesign, we request the RAs continue with the RLG format for the remainder of the detailed design. We propose a parallel working group that will focus on developing an appropriate product design for the RO. The RLG for the ETA and Building Blocks work streams has been mutually beneficial for RAs and participants, and the healthy debate at the previous meetings have led to positive solutions to a number of topics. We believe the

In the meantime, should you have any queries you would like to discuss, please do not hesitate in making contact on the details below.

Brian Kennedy
Senior Power Markets Analyst
Ph: 00 353 1 643 0820 | Email: bkennedy@gaelectric.ie