Electric Ireland Response:

Integrated Single Electricity Market (I-SEM)

Capacity Remuneration Mechanism
Detailed Design – Second Consultation Paper

SEM-15-014

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electric Ireland

1. RESPONDENT'S DETAILS

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2. GENERAL COMMENTS

Electric Ireland welcomes the opportunity to respond to this second Capacity Remuneration Mechanism (CRM) Consultation. Consistent with our previous responses, Electric Ireland views these consultation proposals from the perspective of a standalone supplier and as a representative of the customer.

We are keen that the proposed CRM design should operate effectively and achieve its aims, in particular for the CRM to satisfy an appropriate security standard at an efficient cost and provide efficient signals for market entry and exit as required. Given the decisions from the first consultation, in particular on a split market reference price, the CRM design is already complex and some of our preferences in this response seek to avoid this design becoming even more complex and likely more costly.

In light of the SEMC decision to implement administered scarcity pricing, we strongly believe that the current SEM value of lost load should not be 'rolled over' to determine BM energy prices in the I-SEM but instead, given market coupling, the full level of ASP should be made consistent with that of GB. In addition, we believe there should be a transitional period to enable I-SEM participants to adjust and invest to enable flexible responses to the new price signals.

Also given the SEM Committee decision on ASP, Electric Ireland welcomes the decision to include a socialisation fund which should fully protect suppliers and customers from extreme prices. However it remains to be seen whether customers pay an efficient price for such an 'insurance premium'. The charge on suppliers to generate the socialisation fund is likely to be volatile from year-to-year and creates a significant source of pricing risk for suppliers offering fixed-price terms to customers. Given that the potential drivers of the socialisation fund (listed in Appendix E of the CRM 1 Decision, but excluding potential contributions from the selected Interconnector Option) are not caused by the demand side, we suggest that a separate supplier charging method be considered for the socialisation fund (potentially a flat charge per kWh) rather than assuming it should also be recovered disproportionately from residential 24hour customers in focussed periods like the main CRM charge.

We welcome the proposal to adopt the 'tariff year' as the capacity delivery year in preference to the current calendar year. This aligns capacity with other cost components and will assist in reducing customer pricing risk as well as potentially improving capacity cost efficiency.

We believe that direct trading of ROs better maintains security of supply and the intent of the Reliability Options. However we are not convinced that a centralised market to facilitate Secondary Trading is feasible or desirable for Go-Live.

In the sections on detailed Reliability Option Design it is difficult to know how best to respond to questions relating to e.g. the compartmentalisation of capacity providers into 'new', refurbishing', and 'existing' without knowing about how these categories might compete against each other in the auction design to be consulted on later. Consequently we feel it may be necessary to review these ideas in the context of auction design proposals.

In regards to interconnector and cross-border participation, we believe that the performance-based interconnector-led option is superior on the grounds of consistency and equity of treatment with GB, complexity and cost. We believe that it is preferable to start I-SEM with this relatively straightforward option and monitor the development of the regional balancing market envisaged in the Electricity Balancing Network Code which may provide sufficient price-based incentives for overseas capacity providers to deliver 'balancing services', including across the interconnectors, during periods of I-SEM scarcity.

In addition, Electric Ireland strongly supports fundamental modelling of the European Power System across a number of scenarios on an initial and an enduring basis since it is essential that de-rating values for interconnectors are calculated for both I-SEM and GB capacity markets using a common assumption base to address the issue of equity of treatment.

In our response we focus on those areas that particularly impact complexity, costs, and outcomes for supplier businesses and customers. Consequently, Electric Ireland have largely favoured the more straightforward of the CRM options presented which promote transparency, predictability, liquidity, and reduced costs and risks.

Overall, customers should expect a significant reduction in the cost of I-SEM capacity. It is important that the CRM is designed to achieve an efficient cost of capacity given the other value streams that are being developed for generators.

3. RESPONSE TO QUESTIONS

3.1 Section 2 – Interconnector and Cross Border Capacity

Electric Ireland's overriding concern is that there is equity of treatment between participants in the I-SEM and GB in relation to capacity markets. There should be a high level of consistency between the neighbouring markets which would support the aims of the Internal Energy Market and address EU State Aid concerns in relation to capacity markets. This principle informs both our preferred option and the approach to determining de-rating factors.

Electric Ireland's preferred option is the performance-based interconnector-led option. This supports consistency of treatment since GB have also adopted an interconnector-led approach. Its other benefits are listed in section 3.1.1 below.

We believe it is superior to the other options because:

- While the 'net off demand' option has the benefit of low cost and simplicity it is unlikely to be an enduring solution since it doesn't enable overseas participation and so may not meet State Aid requirements;
- The FTR-led option has the serious flaw of requiring participants to hold FTRs four years ahead or else only allows overseas participation in year-ahead (refinement) auctions;
- The provider-led and hybrid options while offering stronger delivery and investment incentives are very complex, on some points potentially unworkable, and likely costly to implement and manage.

While the (performance-based) provider-led and hybrid options seek to replicate the incentives which are features of the I-SEM Reliability Options and the split market reference price, this is very challenging to achieve in the context of the GB market with different arrangements. We believe that it is preferable to start I-SEM with a simpler solution (performance-based interconnector-led) and monitor the development of the regional balancing market envisaged in the Electricity Balancing Network Code which may provide sufficient price-based incentives for overseas capacity providers to deliver 'balancing services', including across the interconnectors, during periods of I-SEM scarcity.

3.1.1 A) Which of the approaches to the treatment of cross border capacity do you prefer and why? (For the Provider Led and Interconnector Led approach, please specify whether you prefer the "Performance based" or "Availability Based" variant).

Electric Ireland's preferred option is the interconnector-led option (performance-based). This supports consistency of cross-border treatment since GB have also adopted an interconnector-led approach. It provides an additional incentive for the interconnectors to be available and is less complex than some of the other performance-based options. Consequently this option scores high on cost and practicality grounds.

Electric Ireland favours the pro-rating to metering approach to apportion contracted amounts in DA and ID timeframes to individual interconnectors. Differential loss factors are likely to mean differential utilisations on the two existing interconnectors so that the 'balancing utilisation' approach is not appropriate and neither is the complex power flow modelling approach on feasibility, timeliness, complexity, and cost grounds. Electric Ireland believes that the pro-rating approach can be implemented straightforwardly on a low additional cost basis.

From a supplier perspective, the performance-based option would mean that difference payments were paid during scarcity events up to the full de-rated capacity of the interconnectors thus supporting the intent of the Reliability Option in providing a supplier hedge without exacerbating the 'hole in the hedge'. The socialisation fund is claimed to fully fund difference payments to suppliers but it is likely to be very volatile year-on-year and will be a significant source of pricing risk for suppliers.

On the other hand, the availability-based interconnector-led option would only make difference payments for e.g. 3% of the time (when the interconnector was unavailable) and would potentially seriously exacerbate the 'hole in the hedge' problem. In general performance-based options are preferred in principle in keeping with the high level design decision to move away from the SEM availability-based capacity mechanism.

The performance-based interconnector-led option would strengthen the investment signal for interconnectors since additional revenues are provided if available although this is reduced to the extent difference payments are required and not offset by I-SEM / GB price differences. Since interconnector owners (being classed as transmission system operators in the EU Network Codes) are discouraged from having direct interests in the energy market, the direct contracting described in the Consultation Document between the interconnectors and overseas capacity providers is not feasible.

3.1.2 B) Should the de-rating of interconnectors be based on historic performance, or include forward modelling to project how its performance could change in the future?

Current interconnection potentially could represent a significant contribution to I-SEM security of supply: for the GB December 2015 auction, DECC de-rated exports from I-SEM to GB, at times of scarcity, to 6% of the interconnector capacity – the de-rated value for the interconnectors for *imports* into I-SEM from GB could be significantly higher. Furthermore there is the possibility that further interconnection could be built.

Electric Ireland strongly supports the approach of fundamental modelling of the European Power System across a number of scenarios since:

- the alternative is not a valid option now: making adjustments to existing SEM flows to address the many changing factors would be spurious and lack credibility;
- it is essential that de-rating values for interconnectors are calculated for both I-SEM and GB capacity markets *using a common assumption base* to address the issue of equity of treatment – this will include:
    - common assumptions about the likelihood of scarcity in each market both separately and simultaneously (e.g. through common winter high pressure conditions: low temperature and low wind);
    - common assumptions about interconnector availability;
    - common assumptions about the I-SEM and GB energy pricing arrangements (including for the BM); and
    - consistent demand, fuel price, and generation scenarios in each market.

This approach is more likely to deliver consistent (if not equal) de-rating factors for imports to, and exports from, the I-SEM and so more equitable treatment within neighbouring capacity markets. Over time, such models can be checked against actual I-SEM / GB historical flows so as to improve their accuracy and also be updated to reflect regional balancing market arrangements as anticipated by the Network Code on Electricity Balancing.

3.1.3 C) If there is a preference for the "Interconnector led performance based" approach there will be a need to allocate total interconnector flows between specific interconnectors. Which of the specific approaches set out in 2.4.6 do you prefer?

Electric Ireland's preferred option is the performance-based interconnector-led option (see section 3.1 above). Electric Ireland favours the pro-rating to metering approach.

3.1.4 D) If there is a preference for the "FTR led" approach, which of the specific approaches set out in 2.4.15 (net or gross) do you prefer for the allocation of non-day-ahead flows?

Electric Ireland does not prefer the FTR-led option (see section 3.1 above).

3.1.5 E) If there is a preference for the "Performance based Provider Led" approach, which of the specific approaches set out in 2.4.25 do you prefer for the allocation of intra-day and balancing market trades?

Electric Ireland does not prefer the provider-led option (see section 3.1 above).

3.1.6 F) If there is a preference for the "Hybrid" approach:

- Should this be paired with the "Delivery Based" or "Availability Based" provider led approach?
- Should Interconnector participation be mandated or voluntary?

Electric Ireland does not prefer the Hybrid option (see section 3.1 above).

3.2 Section 3 – Secondary Trading

3.2.1 A) Do respondents agree that direct secondary trading of Reliability Options should be permitted?

Electric Ireland believe that direct secondary trading of Reliability Options should be permitted. Direct secondary trading of reliability options has the benefit of ensuring that all obligations held by the original RO holder are transferred to the new capacity holder so that overall delivery incentives on capacity providers as a group are maintained. In particular this guarantees that the new RO holder is physically backed and is incentivised to be available during times of scarcity in the balancing market and earning revenues to offset against difference payments. This in turn will safeguard against volatile balancing prices due to scheduled outages.

This requires that secondary trading is restricted to those capacity providers who have prequalified as per the original auction process. Direct secondary trading also facilitates robust reallocation of credit cover and settlement obligations reducing the risks of bad debt which could also impact on the socialisation fund.

3.2.2 B) Should secondary trading of Reliability Options be via an organised secondary platform? If so, which one of the options is preferred?

Electric Ireland favour option 4: "no centralised market for go- live".

Electric Ireland cautions the development of a centralised market and whether the costs (which will be ultimately borne by customers) of this development are justified at this time considering the following:

- the requirements of secondary trading system are unknown, which could ultimately lead to an overly complex expensive development of a premature trading platform which may not realise the benefits anticipated by participants;
- GB is a larger system that does not have a centralised system, therefore as a small system, is a centralised platform necessary?
- the volume of trades through a centralised platform could be limited;
- the scope to be delivered of Go-Live is already extensive: Electric Ireland believes where possible and practical certain work packages should be de-scoped until after Go-Live, developing a centralised system is such a piece of work;

- REMIT provides participants with knowledge of which providers are on outages at specific times, participants will be able to use this information to contract bilaterally and therefore do not require a centralised market for this.

It is important that when a secondary trade is executed the Capacity Market Operator is notified of RO obligation change to allow for efficient credit cover and settlement reallocation. However a simple email to the market operator instead of complicated centralised market would suffice where a register of potential capacity providers is developed at the pre-qualification stage.

3.2.3 C) Do respondents believe that "back-to-back" trading to lay-off exposure to difference payments should be permitted?

Back-to-back trading may erode security of supply where the secondary trade was with a player with no physical capacity in the market. We support restricting secondary trading to pre-qualified parties as stated above and believe that back-to-back trading should be discouraged.

3.2.4 D) With respect to the creation of a centralised Reliability Option secondary market platform:

- I. Is there likely to be sufficient demand for secondary trading to justify the cost of the development of a centrally organised platform;

Electric Ireland are cognisant that the costs arising from the development of a centrally organised platform will ultimately be borne by the customer, therefore it is imperative that this is not done lightly or prematurely. For that reason, Electric Ireland favours option 4: "no centralised market at go-live". Electric Ireland also believe that the demand and the volume of trades through a centrally organised platform will be low naturally at the start of the market, this affords the market time to develop a centralised market after go-live if required.

II. Do respondents think that capacity providers should be allowed to acquire Reliability Option volume in excess of their de-rated capacity (plus the tolerance margin), and if yes, how the limit on Reliability Option volume for the net primary and secondary volume should be structured?

Electric Ireland believe that participants should be restricted to trading only their de-rated capacity because:

- this rating was decided upon to allow for *unplanned* outages, which are still possible;
- allowing providers to secondary trade to their full name plate capacity is reducing the security of supply since the replacement capacity is provided at a lower level of

confidence – reliability is diluted. If many such trades are done in the summer outage season, then overall security of supply is reduced.

Non RO-contracted plant should be free to offer volume into the secondary trading market. However it is important that they prequalify.

- III. What limits should be placed on secondary trading timeframes, including: the timing of secondary trade execution - how soon after the auction should they be allowed, and how late in relation to real time delivery should they be allowed; and the length of the Reliability Option contract which can be traded?

Electric Ireland have no preference as to how soon after an auction secondary trading should be allowed. However the timeframes chosen close to real time should be achievable in terms of reallocating the RO obligations to the new RO holder which guarantees that there is no settlement or credit cover responsibility ambiguity and in particular sufficient to allow the new holder to post appropriate collateral. Electric Ireland would deem it unacceptable for any arising shortfall to be recouped from the socialisation fund instead of bad debt recovery procedures.

- IV. Should the Capacity Market Delivery Body maintain the processes and capability to undertake pre-qualification throughout the year, and what service standards are required for processing new applications?

Electric Ireland believe that the prequalification process should be maintained throughout the year to ensure the timely transfer of RO obligations to new RO holder.

- V. Should a secondary acquirer of a Reliability Option start from a zero position against each “stop-loss” limit, or should the loss transfer?

Electric Ireland believe that the secondary acquirer of a Reliability Option should start from a zero position against each “stop loss” limit. Secondary trading excluding the transfer of remaining stop loss limits will allow better price transparency where the value of the secondary trade is not polluted by to what extent the original stop loss limit is spent. The new acquirer of the RO will have his difference payment obligation and risk bounded by the original stop loss limit.

Electric Ireland are concerned that if stop losses are transferred as part of the secondary trade, that trades of ROs nearing the upper limit are more valuable as a new acquirer may wish to hold the RO as the stop loss limit is spent allowing freedom to drive up the price in the BM without the obligation to make difference payments. This would impact significantly on the socialisation fund.

The original RO holder's stop loss limits should be frozen at the time of the secondary trade. Once the original RO holder's obligations are reinstated (in cases where the secondary trade is temporary), its limits should not be re-zeroed and should recommence where they left off before the trade.

3.3 Section 4 – Detailed Reliability Option Design

3.3.1 A) Principle of Longer Term Reliability Options:

- Do respondents agree that plant requiring significant investment should be able to avail of longer term Reliability Options?

Electric Ireland is of the view that reliability options of longer duration should be available for plant requiring significant investment however it is important that a balanced approach be struck to safeguard that:-

- the risk that customers pay for stranded capacity in future years is minimised; and
- the risks of participation are not so prohibitive that new investment is discouraged from entry into the capacity market as and when it is required.

Consideration must be given to ensuring efficient entry and exit signals for capacity going forward, but also ensuring that the financial risk is not unduly placed on customers. Allowing the longer term reliability options to extend to the full economic life of a plant places excessive risk on the customer. A balanced approach to longer term reliability options spreads the risk to both the customer and the capacity provider i.e.

- Customers are not saddled with long term reliability options where market conditions are undergoing rapid change.
- Allows for new capacity providers to lock in revenue for a significant proportion of their economic life with the possibility of future capacity revenues where competitive via participation in future auctions.

- Do respondents agree that existing plant should be restricted to reliability options with a term of 1 year?

Electric Ireland is of the view that existing plant would participate in auctions for one year terms as this would promote:-

- Correct entry/ exit signals for existing capacity.
- Accurate price signal for customers.

It is unclear as yet exactly how new capacity versus existing capacity will be allowed to compete in the auctions. From Electric Ireland's perspective, it is paramount that the impact to customers has a strong bearing on the decision. In this thinking achieving value for the customer is paramount and fundamental to the concept of competitive auctions obtained through securing capacity via new providers where this is competitive against existing capacity or via refurbishing existing capacity where this is competitive against procuring new capacity.

- Do respondents believe that longer term Reliability Options should only be available to new-build plant, or should also be available to existing plant where significant investment is being made to enhance or maintain its capability to provide capacity?

Electric Ireland is supportive of the view that longer term reliability options be offered to existing capacity but as with new capacity reliability options, a balance must be struck to ensure protection for the customer.

Refurbishment of an existing plant may be a more economic approach to the delivery of capacity than outright investment in new capacity.

The length of these reliability options awarded to refurbishing capacity should be of a shorter duration than the longer term options offered to new providers as the level of investment required is reduced. In this instance, 3 years as per GB would sound reasonable.

3.3.2 B) Classification of plant as new, upgrade or existing

I. Do respondents have a view on which approach should be used to classify capacity providers as "new", "upgrade" or "existing"?

Electric Ireland's preferred approach is to use the cost threshold as a means of determining the appropriate category of reliability option. We are of the view however that the TSO should have the ability to challenge these costs during the pre-qualification stage where discrepancies were observed from market benchmarks.

II. Do respondents prefer the approach of classifying providers as "new", "upgrade" or "existing", please indicate your view of the criteria, evidence and thresholds that should be used to inform this classification.

Presumably these definitions will enable different classes of provider to compete on an equitable basis. Consequently these classifications will then benefit customers by ensuring they only pay for reliability options of the appropriate length.

3.3.3 C) Maximum available Reliability Option lengths

I. Do respondents have a view on the appropriate maximum Reliability Option lengths that should be available to new-build and upgraded plant?

II. How do respondents view the Reliability Option lengths in relation to the five generic frameworks set out in this section?

Electric Ireland is the view that the **Balanced** options provide capacity providers with the required incentive for entry into the market whilst also safeguarding customers from paying future stranded costs. Longer term reliability options which go out the full economic life of the plant, place excessive risk on the customer paying for stranded capacity in the future.

Stop-loss limits questions

3.3.4 D) Do respondents favour the I-SEM Capacity Year running from October to September, with annual stop loss limits applying over that I-SEM Capacity Year?

Electric Ireland welcomes the proposal that the capacity charge will be based on a 'tariff year' (October to September) with stop loss limits aligning over this period, as opposed to the current calendar year. This will ensure that capacity charges align with other charges in the market and that they are more accurately included in customers tariffs. In addition there are several other important benefits:

- under a tariff year arrangement, annual stop loss limits are more likely to be spent across the winter and less likely to restrict the proper functioning of the ROs during mid-winter whereas under the calendar year approach generators may not have the intended incentive to participate in the reference market and suppliers no hedge against high prices in November and December;
- in any year-ahead 'refinement' auctions capacity providers will have greater confidence in their assumptions for the closer winter period (and less confidence about the second winter period in the calendar year alternative) which may reduce the risk premia included within auction bids and improve the efficiency of the capacity price;

- other charges which make up a customer's bill are scheduled over this timeframe thus having a common arrangement drives simplicity within the market from a customer pricing perspective.

3.3.5 E) Do respondents believe that "per event/day" and "per month" limits are required in addition to the annual stop loss limit?

3.3.6 F) Which approach do respondents favour for the definition of the Per Day/event limit?

3.3.7 G) Please provide views on the appropriate levels for the each of the proposed stop loss limits.

Additional Stop Loss Limits

It is of benefit to the customer that capacity providers who hold reliability options carry the incentive for paying difference payments throughout the whole capacity year since if the stop loss limit is reached, an additional cost is placed on customers via the socialisation fund.

Determining how to profile the annual stop-loss limit across different months or finer defined periods would be challenging (when will the forced outage occur? and may produce a spurious outcome. With this approach, there is a risk of allocating protection to periods where, in the event, it is not required while limiting the protection in some periods where ultimately it is needed. Although just having the annual limits runs the risk of the limit being spent in one big event (and no further protection), it does have the benefit of the limit being used where it is needed in the year.

Uncovered Capacity

Electric Ireland is in agreement that stop-loss limits would only apply in periods of "*uncovered*" difference payments.

Appropriate Level of Stop-Loss Limit

Electric Ireland understand that it is not commercially reasonable for a capacity provider to face potentially unlimited losses for non-performance. However within stop-loss limits, reliability option difference payments act to incentivise capacity providers to perform in all potential scarcity circumstances. Taking this into account, it is the view of Electric Ireland that the limit for the stop-loss limit should be as high as possible i.e. equal to twice the value of the Annual Option Fee. This would:-

- minimise the shortfall in difference payments which fall on customers via the socialisation fund; and
- maximise the incentive for capacity providers to be available.

Commissioning Window and Implementation Agreements Questions

3.3.8 H) Is a period of four years from the Auction Date to the start of the first Delivery Year appropriate?

Electric Ireland is of the view that a period of four years from the first delivery year would appear to be appropriate however as previously stated, it is unclear the methodology that will be employed to determine the proportion of new to existing capacity that will be allocated in the auctions. It is Electric Ireland's first concern that a misallocation to one section could have a detrimental impact on the end user price.

It would also be worth considering here that auctions held well in advance of the delivery date would need be aligned to DS3 system services auctions – costs as yet not covered by a capacity provider in a DS3 auction may be incorporated in the capacity auction bidding.

3.3.9 I) Does setting the Long Stop Date at 18 months after the start of the first Delivery Year strike the correct balance between the costs incurred by the market and the ability for delayed or longer-running capacity projects to be completed?

3.3.10 J) Are the proposed milestones reasonable?

3.3.11 K) Are there any other milestones, especially prior to Substantial Financial Commitment, which could be used to add security to the delivery of new capacity?

3.3.12 L) What proportion of the contracted capacity is appropriate to use to identify Substantial Completion?

3.3.13 M) Is six-monthly reporting appropriate?

3.3.14 N) Do any (or all) of the reports need to be independently verified?

3.3.15 O) Does 18 months provide sufficient time after the Auction Date to achieve Substantial Financial Commitment?

Implementation Agreement Milestones & Reporting

Electric Ireland is in agreement that milestones are critical in ensuring new capacity is ready for an agreed delivery date. Failure to meet new capacity on time will mean the customer would pay extra to cover the shortfall with potentially more expensive capacity options.

Additional milestones and appropriate monitoring can help reduce the possibility of delayed or undelivered capacity. A holistic approach is required to align and streamline the obligations under CRM and DS3 agreements from both TSO and capacity provider perspectives.

Electric Ireland have not commented on the other detailed questions in this section.

3.4 Section 5 – Level of Administered Scarcity Price

3.4.1 A) Which of the options do respondents prefer (and why) for the enduring level of the Full Administered Scarcity Price (FASP)?

- **I. VoLL;**
- **II. EU Consistent (e.g. with GB);**
- **III. Euphemia Cap; or**
- **IV. Existing SEM PCAP**

Ideally the enduring level of the Full Administered Scarcity Price should be set at the value which represents Ireland's end customers' willingness to lose supply. This is a theoretical notion and would take different values were you to ask a big industrial customer and a residential customer or look at different countries in Europe or further afield.

Electric Ireland believes the current SEM value for VoLL lacks credibility and that it is more important, in the context of market coupling, that the enduring level of Full Administered Scarcity Pricing for I-SEM should be set at a level consistent with our EU neighbour, GB, rather than at an independently calculated different value.

At the start of SEM in 2007, VoLL was determined and set at €10,000 using an approximate methodology not based on surveys of SEM customers and has been automatically increased by (harmonised RoI / NI) CPI in each subsequent year to the current value of €11,017.98 (2016) – it has only been used in the SEM to allocate the Annual Capacity Payment Sum to half hours but has not directly set any energy prices - it is not acceptable to roll this over to be used to set a major energy price in the I-SEM without a fundamental review of its value and whether it is appropriate for I-SEM to adopt a markedly different value from its neighbour, GB.

3.4.2 B) Do respondents agree with the definition of full load shedding (when Full ASP applies) as set out. If not please explain why, and your proposed alternative definition.

Electric Ireland supports Eirgrid's Red Alert definition (which is consistent with GB's), but excluding the forecast in immediate periods where there is a high risk of failing to meet system demand or maintaining normal voltage and frequency, defines a full load shedding event:

- System frequency deviates below normal levels; or
- System voltage deviates below normal levels across significant areas of the system; or
- Consumer load has been shed involuntarily.

Since voltage is localised, to avoid a local reduced voltage triggering FASP for the whole system, further definition of the required geographical extent of voltage deviation is required.

Another possible consideration would be a serious / critical event in the interconnected gas network but these might be better treated as leading indicators, potentially to be reported by the TSO, rather than part of the definition of a Red Alert.

3.4.3 C) Do respondents agree that virtual bidding removes any incentives on capacity providers to withhold power from the DAM or the IDM to sell in the BM? Do you agree that this applies regardless of what market power controls are placed on DAM, IDM and BM bids? Do you agree that this applies regardless of the level of the Full ASP? If you do not agree, please explain why.

Participants are likely to have strong incentives to participate in the DAM not least to crystallise the prices set in forward trading and so little incentive to withhold capacity. Holders of ROs will have little incentive to withhold capacity in more extreme circumstances since the net benefit will be capped at the RO strike price. The ability of any party to indulge in virtual bidding does not change these fundamental incentives.

3.4.4 D) If stakeholders consider that it is appropriate to set the Full ASP at a lower level for an introductory period they should also set out, how long that introductory period should be and why, or alternatively the principles that the SEM Committee should employ in deciding when to move from the introductory full ASP to the higher rate full ASP.

Electric Ireland has stated its preference that the introductory level of FASP in the BM should be the same as the cap on Euphemia prices in the DAM – this somewhat limits the potential gains that might be achievable from withholding capacity. When moving to the enduring FASP, this issue should be looked at again in the light of more information about participant behaviour.

Electric Ireland think it is wise that a lower value of FASP is used for the introductory period and that the correct introductory level is the Euphemia value of €3000/MWh for the many reasons given below:

- this value would be a significant step up from the current SEM cap and will provide a sufficiently strong price signal to I&C customers (where it is passed through in contracts) to provide demand response but, as described above, will discourage participants from withholding capacity in the DAM;
- a value of ~€11000/MWh is too big a leap from the current cap (PCAP) of €1000/MWh and would impose inefficient and potentially damaging costs on I&C customers where the price signal is fully passed through and where customers are unable to fully load manage – a telegraphed transition to a higher value would enable customers to make efficient investments to enable full demand response;
- GB plans to transition to Full ASP in a phased approach over 3 years despite having a fully functioning balancing market with historical information - Ireland and Northern Ireland are entering a new market without associated price or behavioural history and should cautiously move to Full ASP over time;
- a high level of FASP could be a barrier to DSU entry in the capacity auctions and could potentially be a State Aid issue given the likely outcome of the SEMC decision being to implement the option 1 / 3 hybrid (difference payment obligation without energy payments) at I-SEM go-live:
    - since the risk of the difference payment obligation at times of scarcity when the DSUs are unable to operate will be significantly increased by a high FASP and likely too onerous (DSUs are at a disadvantage to generators under this model since they cannot earn energy revenues from the ex-ante markets);
    - this is potentially excluding the type of participant that ASP was developed to encourage until such times as the enduring solution is implemented (no timelines offered) where DSU's can earn energy payments for 'foregone consumption' (or use of back-up generation);
- a high FASP will likely lead to providers increasing their auction bids to take account of the higher price risk resulting in higher costs of capital for customers which will be an inefficient cost where customers have no opportunity to respond (see discussion on residential customers below);

- a lower loss of load expectation of 8hours has been selected than our neighbouring markets resulting in potentially more scarcity events than if a higher loss of load expectation of 3 hours had been selected – a lower level of FASP than GB (e.g. €3000/MWh compared to £3000/MWh) would tend to equalise the annual cost of loss of load between I-SEM and GB customers;

- a value less than the Euphemia cap (€3000/MWh) would not be appropriate since it could distort activities both in the market coupled DAM and between the DAM and the BM.

EI believe that the introductory period should not be a fixed period of time but rather the move to the enduring FASP should be based on whether conditions are satisfied such as:

- Electric Ireland believe that the enduring FASP arrangements should only be implemented after significant rollout of the National Smart Metering Programme is complete: supplier charging for capacity in the specified 'focussed periods' will be disproportionally weighted towards residential (24hour) customers (an 11% increased share of the capacity pot compared to the SEM sharing basis) but these customers (and all other NQH metered customers) will have no ability to respond to these strong price signals until smart metering (to measure any demand response) and time of use tariffs (to pass on e.g. capacity price signals) are implemented;

- the SEMC's preferred enduring solution for DSUs has been implemented where DSUs can receive energy payments to offset difference payments on a par with generation;

- a fundamental review of, and consultation on, the appropriate I-SEM VoLL has been completed considering both the appropriate level and any rationale for having a markedly different value to GB; and

- that sufficient I-SEM price and participant behaviour history is available to conduct a full impact assessment of the regulatory change to a higher FASP level on both I-SEM participants and market coupling – OFGEM carried out an extensive Significant Code Review process before deciding to implement administered scarcity pricing in GB on a phased basis on top of the existing fully functioning Balancing Market.

3.4.5 E) If you favour a different level of Full ASP, either for an introductory period, or after any introductory period, please indicate the level and justify your response.

Please see response in section 3.4.4 above.

3.4.6 F) Do respondents agree with the proposed approach of using a static approach to setting the piece-wise linear ASP function at the inception of the I-SEM, and if not why not? If yes, do you agree with the proposed approach of setting the piece wise linear equation as a function of the remaining MW of available operating reserve?

Electric Ireland think that using a static approach to setting the piece-wise linear ASP function at the inception of the I-SEM is sensible – this will likely provide more certainty to capacity providers in formulating their auction bids and reduce the risk of inefficient costs being incorporated into the final capacity cost for customers.

Electric Ireland supports the price being determined as a function of the remaining MW of available operating reserve. Electric Ireland agrees with the principle that the piece-wise linear function should follow the shape of the LOLP function to the extent possible.

Electric Ireland believe that the provision of good forward forecasts by the TSO of scarcity conditions, in addition to Red & Amber Alerts and immediate market notifications of outages, are as important as the setting of Administered Scarcity Prices. Rolling half hourly forecasts for a 4-hour forward horizon of capacity margin, remaining operating reserve, and forecast ASP will enable market participants including DSUs to prepare (perhaps by re-declaring availability and BM offers) and reduce response times thereby increasing the capability to respond to a scarcity event. This is most relevant for emerging scarcity events driven by high demand and low wind where a reasonable forecast of conditions a few hours ahead can be made. Scarcity events driven by plant forced outages have less scope for pro-active remedies.

Where good forward information is available it is appropriate that the piece-wise linear function is relatively flat where e.g. >80% of the target operating reserve remains but that the price level increases rapidly when less than 20% remains.

3.4.7 G) What should the value of X in Figure 12 be?

Ireland believe that X should not be fixed but instead be set dynamically to equal or exceed the RO strike price as indexed by gas and oil. Given the intention to set this strike price high, setting X above or equal to this strike price will not distort BM bidding. Participants, subject to market power decisions on SRMC bidding, may be able to reflect emerging scarcity conditions in their BM bids and offers potentially encouraging a response that avoids ASP being triggered.

Equally, setting X at or above the RO strike price level means that suppliers and customers are protected through difference payments against the most extreme prices. This is valid since, until significant rollout of smart metering is delivered, the vast majority of mass-market customers will have no way of responding to such price signals.

3.4.8 H) How far in advance of the start of the Capacity Delivery Year should the piece-wise linear function be set. Does this need to be before the T-1 auctions?

This would need to be delivered at least a few months prior to the T-1 auctions, to allow providers to factor these parameters into their calculation of their capacity auction bids.

3.4.9 I) Do respondents think that any changes need to be made to the governance of the target operating reserve policy. If yes, what are these changes?

Given that the target operating reserve levels will influence how quickly energy prices will rise to the introductory / enduring FASP level as well as system security, it is essential that a broader governance arrangement be put in place. Electric Ireland believes that these should be treated similarly to any of the other T&SC parameters which are subject to annual consultation and SEMC decision. Such a process will allow market participants to comment on the values proposed by the TSOs on system security grounds.

In addition, given the changes to operating reserve services under the DS3 Programme there are also questions of definition to be considered in order to implement the ASP proposals robustly.

3.5 Section 6 – Transitional Issues

3.5.1 A) Which of the suggested options (annual auction, block auction, do nothing) do you prefer?

Electric Ireland's preferred option is Option 1 (Auction Separately). This option allows for improved price discovery and the process is straight forward and transparent.

While the SEM is currently in a condition of oversupply of capacity, looking forward there is considerable flux in the system: units in NI potentially closing due to emissions limits; uncertainties over timelines for build of the 2nd North-South tie-line; and uncertainties over the build of new renewable generation in the context of REFIT 2 ending and changes to connection policies. Consequently Electric Ireland favours Option 1 where updated information can be reflected in annual auctions during this period of flux rather than capacity procured in a block under Option 2 in 2017.

Electric Ireland have several concerns over Option 2 (Auction as a Block) as it is a less transparent approach and that it may lead to inappropriate capacity procurement at the start of a new market in a condition of significant flux and which may lead to excessive capacity payments by customers.

3.5.2 B) If you prefer the do-nothing auction, do you believe this should be accompanied by relatively low levels of Administered Scarcity Price?

This is not a realistic option and would seek to enhance the perception of regulatory risk among potential investors in Ireland and Northern Ireland.

In addition, in the context of the intention to accommodate significantly more intermittent generation running on the system (SNSP limit to 75%), significant investment is required to deliver ancillary services provision from both generation and the demand side. Such a capacity revenue 'holiday' would jeopardise achievement of these goals particularly from new DSU providers (since virtually all DSU revenue currently comes from capacity revenue).

The idea that BM prices could be set administratively at a high level without ROs being awarded and suppliers receiving some protection via difference payments is unacceptable. This also moves away from the concept of a competitive rather than a regulated market: there may be a regional cross-border balancing market established in this time frame under the provisions of the Network Code on Electricity Balancing.

Suppliers would find it very difficult to procure reasonably priced CFD's against the BM to protect against the volatile BM prices.

3.5.3 C) Are there any other transitional issues respondents feel that we should take account of when implementing the CRM?

DS3 auction timetable should be aligned with the CRM auctions. Ideally DS3 auction should take place first (or at the same time) in order to factor any DS3 revenue expectations into capacity bids. The same platform should be used for the CRM and DS3 auctions. CRM, DS3 and energy settlement should allow netting were possible to reduce credit cover requirements.

Consideration should be given to whether the new auction should be held prior to the existing auction as there is a possibility that the auction that is held first will drive the price outcomes in subsequent auctions.

Electric Ireland welcomes the proposal that the capacity charge will be based on a 'tariff year' (October to September) as opposed to the current calendar year. This will ensure that capacity charges align with other charges in the market and that they are more accurately included in customers tariffs. In addition there are several other important benefits:

- under a tariff year arrangement, annual stop loss limits are more likely to be spent across the winter and less likely to restrict the proper functioning of the ROs during mid-winter whereas under the calendar year approach generators may not have the intended incentive to participate in the reference market and suppliers no hedge against high prices in November and December;
- in any year-ahead 'refinement' auctions capacity providers will have greater confidence in their assumptions for the closer winter period (and less confidence about the second winter period in the calendar year alternative) which may reduce the risk premia included within auction bids and improve the efficiency of the capacity price.