



Integrated Single Electricity Market (I-SEM)

Capacity Remuneration Mechanism Consultation Paper 3

Consultation Response from

BORD NA MÓNA 

The logo for Bord na Móna, consisting of a yellow sun-like symbol above a green wavy line, with a red diamond shape at the bottom right.

SEM-16-010

April 2016

Introduction

Bord na Móna (BnM) welcomes the opportunity to respond to the SEM Committee’s Consultation on I-SEM Capacity Remuneration Mechanism (SEM-16-010). BnM would like to commend the RA’s on their comprehensive evaluation of the CRM Auction Design and relevant market examples.

In addition BnM would like to highlight the importance of the CRM revenue stream as a quintessential part of the overall revenues for participants. It is evident from the consultation process to date that there is a substantial degree of change in this work stream, and therefore would like to reiterate the importance of developing a framework that provides long-term security of supply, in a stable and adaptable manner.

Careful consideration will be required on some of the key elements of the CRM, such as price caps and setting strike prices, in order to create a workable balance of risk for efficient capacity providers and allowing for exit of inefficient providers. Given the expectation that scarcity events would be rare, the relevance of price caps and their level must be given due consideration and allow for the recovery of the cost of all generation. It is paramount that the large number of working components do not compromise the overall purpose of the CRM, by placing undue uncertainty on market participants. Transparency on these components will be paramount to both suppliers and capacity providers, including transparency on the impacts, the decision process, whether they are to be consulted on and timelines, in order to provide a level playing field.

BnM comments to the specific consultation components are outlined below.

3.2 Auction Design Framework and Auction Frequency and Volumes

Bord na Mona believes that the proposed approach for the T-4 and T-1 auctions as the enduring capacity solution seems reasonable. The four year lag period, would allow a sufficient timeframe for new development entry and T-1 auctions allowing for closer to real time adjustment of the capacity requirement.

BnM have concerns regarding the proposed approach for the transitional auctions, whereby annual capacity is procured one year out and will not provide a longer term view or security to providers. The timing of these individual auctions (T-1) and procuring the total capacity in one auction could create undue risk for new and existing capacity providers as they will not have future visibility, potentially creating exit signals of efficient if not successful in a given years. BnM believe that the interim auction arrangements should cater for efficient transition to the enduring arrangement and that it would be prudent to run the separate auctions consecutively in the same year (2017), giving more certainty to new and existing capacity providers, allowing for secondary trading and reducing somewhat the treat of unexpected exit of efficient capacity.

Timing of auctions

BnM would have a preferred position of limiting the flexibility of the timing of the T-1 and the T-4 auctions. The proposed nine months of flexibility in lead time places excessive risk on providers. BnM believe that having designated dates for the capacity auctions are paramount, given that capacity remuneration is a key component of revenue for all providers, both existing and new.

Market Power

BnM agrees that there will be a potential for both unilateral Market Power and the potential for collusion, requiring market power mitigation to be implemented in RO CRM Auctions. BnM recognise that the RA's evaluation of the qualified market will be key to establishing how competitive the RO markets are and the capability of the qualified capacity providers to exercise power. BnM would promote a balance between adequate market power mitigation and achieving the long term goals of the capacity market, security of supply. BnM have a number of comments it would like to make:

BnM would agree that the debate on whether existing firm transmission which has opted out of T-4 auctions on the grounds of retiral, should be prohibited from bidding in subsequent auctions is a complex one. BnM would agree that there would be a case for dispensation, if new information becomes available to intermitted plant, that changes the economic circumstances of the bidder would be a valid reason for the change, and allowing all capacity providers to contribute to economic efficiency and security of supply, especially in the first few years of implementation of the RO market, where the risk of plant exit owing to uncertainty may be high.

BnM believe that the market should set the price, however in the case that the exercise of market power may prevent prices falling to reflect the fixed costs of capacity provision BnM would agree that bid price caps may be appropriate in the case of those mandated bidders who fail some dominance test. Should the RA determine that there is a requirement for Price taker offer cap or bids limited on the basis of technology specific going forward costs, BnM would recognise the need for an open and transparent process of setting the price cap. Plants Bids should be allowed to be reflective of the plants costs.

BnM agree that firm transmission access plant should be permitted to bid residual capacity in the T-1 auction, as plants will have a clearer understanding of position closer to real time. Also allowing additional volumes and increased liquidity in the T-1 auctions.

Auction Design

Auction format

BnM would support the multiple round descending clock bid format, to allow for great price discovery, and better information transparency of bid prices, reducing the risk of operating in a new market. And as such would support a bid structure that would cater for this, such as the exit bid approach that was

adapted in GB. Winners would also be determined purely on price offered for each capacity year with no adjustments for contract length.

Lumpiness/discrete bid problem

BnM have concerns regarding the RA's proposal to deal with the lumpiness issue as it places undue risk on capacity providers who are in merit. BnM would contest that allowing bids to be accepted on the basis of merit order is the only equitable approach. BnM is of the opinion that the clearing prices should be accepted based on uniform clearing price for in-merit winners based on the marginal bidder and would not support the proposal to reject bids from a in merit plant.

Sloped Demand Curve

BnM recognise the merits in using a sloped demand curve, representing a more elastic view of demand which allows efficiency gains in price setting allowing for significantly more capacity to remain on the system if prices are low enough, and equally ensuring that the capacity volume reduces if prices are high enough.

However some consideration will be required in determining the many elements of the curve, as there is potential knock on implications of the system purchasing less than the requirement if prices are higher. Progressing on BnM's response to CRM consultation one, the sloped nature of the demand curve could be aligned with neighbouring markets such as GB and France, operating to a nominal 3 hour LoLE. BnM recommend the same security levels should apply for the transitional period.

Price determination.

BnM would agree that it is appropriate to pay all bidders on a pay as clear basis, as it is generally accepted as economically efficient, creating exit signals for out-of-merit bids. In addition pay as bid is typically not possible for BnM's preferred auction format, multiple round descending clock. BnM would not support out of merit winners being paid.

BnM would like to see equitable treatment of tied bids, measures such as those used in GB, ranking exit bids with highest to lowest capacity appear fair.

Information

BnM agree with the RA's proposal for information which is to be provided before qualification, between qualification and the start of the auction and after the auction. BnM understand that there is a need to strike a balance between providing enough information to allow efficient trade and not being in a position of infer information about individual bidders. In light of this BnM would support the total MW of capacity that qualified being available as opposed to the aggregate level results that are published in GB. Proposed restrictions on bidder communications which are aligned with existing competition law appear appropriate.

Auction Parameters

Auction Price Cap

Given the expectation that scarcity events would be rare, the relevance of price caps and their level must be given due consideration and allow for the recovery of the cost of all generation. BnM would contest that the Auction price Cap should be set high or should be removed. Price caps based on a minimum of 1.5 to 2 times Net CONE, as is evident in other markets, should be set. Perhaps in the initial years it could be set at the upper end of the range, with the potential to review and bring to the lower end of the range after a number of years. Given the likely high levels of uncertainty with estimating revenues associated with missing money, the methodology of how price cap and Net Cone is calculated will be key and should be consulted upon with industry.

Bid Limits

Bid limits, should not be set so low as to endanger plant recovering its costs, participants should be in a position of bidding its costs.

Auction Governance, Roles and Responsibilities

Governance

BnM have concerns regarding the development of a number of the key parameters by the TSO, as the CRM delivery body and the transparency of the governance arrangements, which will ensure the stability of the market and consumers interests. Key parameters, such as Net CONE, BNE, and setting of capacity requirement, sourcing fuel prices will all need to be subject to regular consultation and allow input from industry, prior to decision.

Other Residual Issues

Strike Price

The strike price in BnM's view must in all circumstances, be set at a level which will not interfere with the energy market of all units that are scheduled. BnM support the inclusion of all variable costs including carbon costs into the Strike Price calculation.

Month-ahead index

BnM agree it would appear to be administratively simpler to move to a month ahead index, which would maintain the same strike price for each day of the month. More fundamentally we would note, regardless of the index that is chosen, it must cover the total cost of running all generators during any potential period of system stress.

In summary BnM very much welcomed the opportunity to further contribute to the SEM committee's proposals for the transition to a RO detailed design of the Capacity Remuneration Mechanism.

Finally, if you have any queries or require clarification on any point, please do not hesitate to contact me.

For and on behalf of Bord na Móna



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