



# **Integrated Single Electricity Market (I-SEM)**

## **Capacity Remuneration Mechanism CRM 3 Supplemental Consultation Paper – Locational Issues**

### **Indaver Consultation Response**



**SEM-16-052**

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## 1 RESPONDENT DETAILS

Indaver Ireland Ltd currently owns and operates a small, centrally dispatched hybrid renewable generator (17MW registered capacity) in Duleek, Co. Meath. Within the next five years we plan to develop two similar generators in Cork and Belfast. Given the timelines, these facilities could become the first new build/own/operate projects in the I-SEM.

Waste-to-energy hybrid capacity is controllable and predictable, though the operation is driven primarily by waste treatment rather than energy production. The facilities have priority status in the merit order and the Meath facility receives REFIT support on the renewable fraction of output. Merchant revenue comprising energy, capacity and DS3 system services payment, is therefore important for the financial performance of the facilities, particularly for the Cork and Belfast projects where no renewable energy subsidy currently exists.

For these reasons, the area of key importance to Indaver is to have a predictable fair capacity payment for all generation participants given the over-arching supply and demand within the I-SEM. Our plant, existing and future, may both benefit and be disadvantaged given the proposals within the paper given their diverse locations. The unpredictability of capacity revenues is, however, increased for all projects under several of the options considered in this consultation paper. Unpredictable merchant energy revenues reflect themselves in rent seeking in the energy market and DS3 systems services.

There is also material likelihood that one of our facilities may be delivered in advance of the first T-4 auction delivery year. We are greatly concerned that this is not being given adequate consideration within the transitional design as a whole. This has always been of importance to Indaver. We hope the interaction of locational signals and how they may change from a T-1 to a T-4 auction, whether new entrants can secure long-term contracts through a T-1 auction, and the SEM Committee's discomfort in new entrants securing locational value under long-term contracts that there will now be a more considered assessment of the realities facing new entry during the transition phase.

Our comments as set out below focus on these areas.

## 1 CONSULTATION QUESTIONS

### 1.1 OUTLINE OF ISSUE AND PROPOSED SOLUTIONS

Indaver disagrees around the assessment of new entry, and disagree that CRM Consultation 2 sets out any SEM Committee decision that there would/should be no new entry during the transition phase.

Indaver supports the inclusion of a mechanism to resolve locational signals within the overall CRM process, but not any solution which results in:

- distortion of the predictability of the clearing price, i.e. the locational issues should not impact the overall supply-demand signals in the single I-SEM pricing zone,
- the heuristic exclusion (be it through direct decision, or objective execution of an ultimately heuristically determined process) of an in-merit generator.

This would undermine the entire CRM as a mechanism, make revenues highly unpredictable, and will result in higher costs in energy, DS3 system services and/or any other revenue streams available to market participants where possible.

We believe that if locational signals are to be designed, there is little point in partially resolving the issue through the capacity mechanism. What if – for example under Option C – the heuristic rules solved for the identified major constraints (North-South, Dublin) in Step 2 but the TSO was subsequently notified that a further must-not-close generator was going to retire?

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We agree with the high level approach to managing the constraint process, i.e. run an unconstrained auction and determine if there is a shortfall of locational security. Those generators necessary to resolve the locational issue should be protected through a further CRM contract or allowed to set the energy price high through a relaxation of the bidding principles in the balancing market, as appropriate to the situation. There should be no exclusion of in-merit generation and there should be no after the fact distortion of the clearing capacity price in the market.

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## 1.2 AUCTION DESIGN FRAMEWORK

We prefer Option E, whereby an unconstrained capacity auction is performed, and an ex-post security of supply analysis is performed to identify remaining security of supply issues.

We do not believe that in-merit capacity providers should be excluded through heuristics or the market price should be lowered on the exclusion of those participants. Both of these scenarios create unpredictable revenue outcomes for generators which have nothing to do with overall supply and demand within the single pricing zone of the I-SEM.

The main issues raised by the SEM Committee with Option E (with no adjustment of the clearing price or exclusion of in-merit generators) appears to focus on state aid concerns and cost to the consumer. Plant of strategic locational importance to manage temporary constraints should not result in the refusal of State Aid approval for an overall capacity scheme.

In relation to cost to the consumers, the SEM Committee has not evaluated the fact that while securing capacity on the system will be more expensive than it might be under Option E, it is likely to be materially cheaper than currently. The move to an auction based mechanism will deliver savings to the consumer; Indaver questions whether the remaining savings under discussion within the paper are worth distorting the entire capacity market and the predictability of that investment signal for orderly plant exit and entry. Indaver believes a capacity and energy market with efficient entry and exit will yield medium to long term benefits for the consumer in Ireland far in excess of the short-term benefit of making every possible short-term saving at the expense of a coherent market design.

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## 1.3 LONGER TERM CONSIDERATIONS

Indaver is of the view that all auctions (T-1 and T-4) should be unconstrained. Under Option E, the TSO would evaluate security of supply issues and react accordingly, either granting an out-of-merit contract under the CRM or DS3 System Services as relevant and appropriate for the situation.

These potential contracts would be evaluated by the TSO as part of its constraint management strategy, i.e. would a contract for a generator that relieves a constraint be cheaper and more reliably delivered than network build. In effect this would add generators to the TSO tools to manage constraints on the system.

Indaver appreciates that this adds further scrutiny to TSO actions, both in declaring that a CRM auction has delivered a security infeasible result, and indeed on its network plans and success on delivering on same. Further commercial incentivisation around constraints could also be considered as part of this framework.

In that regard, Indaver are suggesting that the longer-term issues will come down to regulatory judgement supported by the advice of a commercially incentivised TSO with bilaterally negotiated contracts.

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## 1.4 LOCAL SECURITY OF SUPPLY AND MARKET POWER

There is much emphasis given in this capacity paper regarding the potential for new entrants to secure long-term contracts that lock in prices reflective of temporary constraints (which last for a

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shorter time than the contract).

If the electrical system is in such a situation, i.e. a capacity issue has arisen due to lack of transmission infrastructure that cannot be resolved without recourse to generation investment, then security of supply issues must over-ride cost to the consumer concerns. This also applies for existing plant seeking to close, but requested to stay on-line until the transmission issue is resolved.

Providing for a set-in-advance ruleset under such circumstances that will apply to all classes of generation in all circumstances that may be needed to resolve the locational issue appears highly restrictive, and subject to extra-regulation negotiation if the price is simply too low, or the ruleset provides for excessive profits for the generator in question.

Having such a ruleset that might not “fit” will only open the possibility for negotiation or dispute while a security of supply issue looms in the background.

As per Invader’s overall position, if the unconstrained capacity market fails to deliver capacity in the correct location the provided offers (for either capacity or DS3) should provide the starting point for any required commercial rate within a long-term contract.

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## 1.5 SUMMARY

While other options presented may have the appearance of providing for an objective process, i.e. a process that has parameters defined ex-ante with an automated process transparently yielding capacity auction winners, Indaver does not believe that such a process will be without material risk. Such risks include still-needed after-the-fact intervention, or challenge on the initial “objectivity” of the rules within the process itself. Simply put, adding locational signals to the capacity mechanism when scarcity is defined by an all-island administered scarcity price will struggle to avoid heuristics, i.e. Option E as an ultimate fallback.

Indaver supports Option E with no distortion of the all-island capacity signal, no exclusion of in-merit generators in the auction, and with CRM or DS3 contracts (of the appropriate length) provided as necessary and appropriate to resolve security of supply issues as they arise under either the T-1 and T-4 auctions results.