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Generation & Wholesale Markets

ESB GWM Response:

**CRM State Aid Update, 2019/20 T-1 Capacity Auction Parameters
and Enduring Storage De-rating Methodology Consultation Paper
(SEM-18-009)**

19th April 2018



Contents

1. Introduction.....	1
2. Executive Summary.....	1
3. Main Comments	1
3.1 Review of CY2018/2019 CRM T-1 Auction	1
3.1.1 Existing Capacity Price Cap (ECPC)	2
3.1.2 Technology classification for de-rating factors	2
3.2 Impact of CRM T-1 Results.....	3
3.3 Future Auction Format	4
3.4 Timing of Interim Auctions (CY 2020/21 & CY 2021/22)	4
3.5 CY 2019/20 Auction Parameters	4
4. Response to Consultation Questions.....	5
4.1 Auction Timings	5
4.2 CY Parameters	5
4.3 De-Rating Factors	5
4.4 Appendix: De-Rating Factor Calculation Methodology	6
4.5 Long Stop Date.....	7

1. INTRODUCTION

ESB GWM welcomes the opportunity to respond to the CRM State Aid Update, 2019/20 T-1 Capacity Auction Parameters and Enduring Storage De-rating Methodology Consultation Paper (SEM-18-009). The consultation covers a wide range of aspects relating to the EC state aid decisions, future CRM auction timings, CY 2019/2020 Auction parameters, De-Rating Factors, and modifications to the Long Stop Date and Termination of New Capacity.

The structure of this response is broken into three sections; the first details ESB GWM's main comments in relation to the Capacity Year (CY) 2018/2019 Auction and future auctions. The second section lists ESB GWM's answers to the consultation questions. The third section provides a summary of this response.

2. EXECUTIVE SUMMARY

The key points ESB GWM want to raise in this response can be identified under the three heading:

Processes:

- ESB GWM request any consultation for the future auctions to be allocated the standard six week consultation period.
- ESB GWM believe a review of the CY 2018/2019 T-1 CRM Auction will enable the improvement of the CMC and efficiency of future auctions. Considering the results of the CY 2018/2019 Auction and qualification process, a review of market participants would be beneficial in identifying market participant's perspective of the workload due to the ECPC being set at 0.5 x Net Cone.

CY Parameters:

- In relation to the tight timelines around the interim auction periods, the methodology applied to the previous capacity payment mechanism, in terms of annual revisions, should be applied to the CY 2019/2020 auction parameters (APC inflation).
- The setting of the ECPC at 0.5 x Net Cone needs to be reviewed to ensure the environment to promote a competitive auction that will allow the formation a market drive price.

Efficiency:

- Further clarity on a targeted mechanism available to auction losers is required to provide the transparency required for the CY 2019/20 qualification process.

3. MAIN COMMENTS

3.1 [Review of CY2018/2019 CRM T-1 Auction](#)

ESB GWM consider a review of the T-1 CRM Auction held in December 2017 for CY 2018/2019 would be a beneficial process to the Regulatory Authorities (RAs) for further developing the Capacity Market Code (CMC) by building on the experiences of the market participants. Furthermore, a review of the systems,

processes and timings through the participants feedback could have been factored into this consultation and applied to the execution of the next two interim auctions (CY 2020/21 and CY 2021/22). ESB GWM would like to take this opportunity to provide its feedback on the first T-1 CY 2018/19 CRM Auction. The main feedback on the first T-1 CRM Auction is:

3.1.1 Existing Capacity Price Cap (ECPC)

In the CRM Parameters decision paper (SEM-17-022), the rationale provided by the SEMC to set the ECPC at 0.5 x Net Cone was to reflect two key functions¹ (1) the ability to limit market power and (2) not place an excessive workload on the RAs and market participants. Feedback from market participants on the implementation/impact of the two key functions may ensure regulatory intervention is set at a level that encourages competition in the CRM so that it doesn't negatively impact on the efficiency of the market or the creation of appropriate entry/exit signals. Considering the results from the T-1 CY 2018/19 CRM Auction² and the reasoning set out in the decision³ to base the multiplier for the ECPC at 0.5 x Net Cone, ESB GWM suggest a review of the 0.5 multiplier prior to the next auction.

ESB GWM are of the view that the market may achieve a truer market price that is not impacted by market power through a review of the ECPC. As per 6.3.33 of the CRM Parameters consultation (SEM-16-073), the rationale for setting the ECPC at 0.5 x Net Cone is that if set at this level, the SEMC estimated that almost all of plant required to meet the Capacity Requirement could bid its Net Going Forward Costs (NGFC) without needing to apply for a unit specific bid limit and "*that it is important that the ECPC is not set at a level significantly above where [the SEMC] expect the market to clear in current market conditions*". Since the CRM auction results had a clearing price above the ECPC, it would appear the ECPC seems to determine a regulated price rather than allowing the formation of a market driven price under competitive conditions in the CRM auctions. A fully competitive market will create the correct prices that act as temporal signals for entry and exit. Whereas, the creation of a regulated auction price could artificially prevent the auction from providing the correct signals to investment from new and incumbent participants.

The second key function of setting the ECPC at 0.5 x Net Cone was that it would not place "*an excessive workload on the RAs and market participants*"⁴. In this consultation paper (SEM-08-009) the SEMC stated "*the workload on the RAs and the market participants resulting from the number of USPC applications, whilst challenging, was manageable*"⁵. ESB GWM are of the view that an industry review of the CRM CY 2018/2019 would be useful for determining market participants views on the workload due to the ECPC being set at 0.5 x Net CONE.

3.1.2 Technology classification for de-rating factors

The current classification of "Gas Turbine" and "Steam Turbine" is ambiguous for participants seeking to qualify plant that consist of both i.e. CCGT units. The impact the different classification can have on the de-rating factor of a plant can be significant. ESB consider a capacity market unit consisting of a gas and steam turbine should be able to determine a dual de-rating using the "Gas Turbine" and "Steam Turbine" classification or a reclassification of the technology class similar to GB's Capacity Market technology (i.e. CCGT, OCGT etc) is required. Not allowing market

¹ Point 6.3.101 of SEM-17-022.

² ECPC was set at €41,060 and the Auction Clearing Price was set above the ECPC at €41,800.

³ SEM-17-022

⁴ SEM-17-022

⁵ Point 4.5.4 of SEM-18-009.

participants to apply the defined classifications is preventing the true benefit from the technological advantages of CCGT unit being achieved.

In summary, ESB GWM consider the outcomes of the auction qualification process in conjunction with the auction results necessitate a review of the ECPC being set as 0.5 x Net Cone. Furthermore, ESB GWM request a review of market participants feedback be performed prior to the next interim auction CY 2019/20 and any subsequent auction where a material change has occurred to the auction format.

3.2 Impact of CRM T-1 Results

Following the results of the CY2018/2019 CRM auction, a number of participants requested a derogation⁶ from the grid code three year notice period. ESB GWM would welcome consideration of the consequence of any derogations and their related side-contracts on the efficient design and functioning of the subsequent round of annual auctions and impact on unhappy auction winners.

The lack of transparency involving the targeted mechanism for CRM losers that need to be retained for system reasons could undermine the CY 2018/19 auction results. ESB GWM are concerned that the targeted mechanism could have unintended consequences that would put its strategic plans at risk through the creation of regulatory uncertainty and the potential to create greater missing money issues. The transparency of the derogation status, which lends regulatory certainty, is crucial to all market participants prior to the CY 2019/2020 qualification processes. Any TSO/RA decision that results in a change to the current generation portfolio's market participation status could impact on market participants' decision for future plant overhaul / upgrades required for the relevant capacity year. The potential impact of plant exiting the market and/or the system needs to be fully incorporated into market participants upcoming auction qualifications processes.

ESB GWM believe the regulatory uncertainty around the treatment of non CRM contract holders has the potential for perverse outcomes for competitive market participants. The CRM Parameters decision prevented market participants from submitting all their investment costs into a single auction offer and directed market participants to allocate a proportion of their investment costs across a number of single auction USPC application (over the investment recovery period). This is a high risk requesting market participants to structure their bids for each auction (over the investment recovery period) while taking into consideration the exit signals to auction losers. Even though EirGrid have published the Generation Plant Closure Process document market participants face a significant amount of regulatory uncertainty and commercial risk going into the CY 2019/20 qualification process due to the lack of detail regarding the potential targeted mechanism for plant required for system reasons and the processes involving the plant for future CRM auctions.

ESB GWM would like to use this opportunity to request further information on the status of current derogation applications in advance of the CY 2019/20 qualification deadlines.

⁶ <http://www.eirgrid.ie/newsroom/capacity-market-auction/index.xml>

3.3 Future Auction Format

ESB GWM recognize that the SEMC have identified May 2018 as the period for a consultation on the future auction format. However, ESB GWM would like to take this opportunity to provide some input into this consultation.

Following the outcome of the CRM T-1 Auction, ESB GWM consider a multi bid/combinatorial format is required to ensure the integrity of the auction results is upheld. While two units on the same site can operate separately, in some cases they share a significant amount of equipment. Therefore, the splitting of costs between the units is largely an apportionment rather than costs actually arising distinctly at each unit. In particular, ESB GWM would like to discuss in the May consultation⁷ the possibility of aggregating units greater than the de-minimis threshold on an exceptional basis with RA approval.

ESB GWM would request the May consultation is allocated the necessary six week consultation phase considering the importance of the enduring auction format and potential inclusion of transmission capacity constraints.

3.4 Timing of Interim Auctions (CY 2020/21 & CY 2021/22)

The consultation proposes to hold the transitional auctions for CY 2020/21 and CY 2021/22 at the same time, around December 2019. Considering the need to abide by the Capacity Market Code tight timelines for holding the interim auctions and the first T-4 auction, ESB GWM believe holding the remaining transitional auctions (CY 2020/21 and CY 2021/22) in December 2019 is feasible. ESB GWM believe a review of market participant's assessments of the CY 2018/2019 qualification processes and potential workload implications for completing two CY CRM qualifications in such a short period of time would assist participants in identifying improvements to the workload requirements for holding the two remaining transitional auctions simultaneously.

3.5 CY 2019/20 Auction Parameters

The SEMC have proposed to make very little changes to the parameters used in the CY 2018/19 auction. The main parameters that are proposed to change are the Capacity Requirement and De-Rating values. The SEMC is minded to not change the APC, ECPC and USPC in the short term but do commit to carrying out a full review in advance of the first T-4 capacity auction. ESB GWM believe that waiting for the T-4 auction is too late and the opportunity to get an efficient outcome needs to be reviewed now.

ESB GWM's view is that the Net CONE should be revised similar to the methodology applied in the existing SEM Capacity Payment Mechanism (CPM) i.e. the application of an yearly inflation index. The retaining of this existing methodology should not require the same level of detail provided in the CRM parameters consultation. Thus, in light of the tight interim auction timelines and ensuring regulatory certainty around the capacity market, ESB GWM consider it prudent and efficient to apply a similar CPM inflation methodology to yearly deviations in the CRM auction parameters for the remaining interim auctions. The minded to position to not implement any inflation element is a change from an industry accepted procedure which only serves to introduce regulatory uncertainty for existing market participants and potential new investors.

EirGrid's All Ireland Generation Capacity Statement 2017-2026 estimate an increase in installed wind capacity of approximately 300 MW from 2018 to 2019. ESB GWM consider this increase of installed wind

⁷ Point 2.2.10 of SEM-18-009

capacity could have a considerable impact on the calculation of the Net Going Forward Costs (NGFC) used in setting the APC multiplier for the ECPC (currently set at 0.5 for CY 2018/19 and proposed to remain the same for CY 2019/20).

ESB GWM consider a further review of the proposed CY 2019/20 auction parameters in this consultation may be required if any regulatory decisions influence market participant's CY 2019/20 auction qualification or the CY 2019/20 auction parameters i.e. capacity requirements.

4. RESPONSE TO CONSULTATION QUESTIONS

4.1 Auction Timings

Q. Do you have any comments on the indicative auction timetable set out in this section?

A. ESB GWM view the indicative auction timetable for the CY 2020/21 and CY 2021/22 transitional auctions as achievable depending on the auction parameters and qualification processes. ESB GWM consider a review of market participant's experiences of the CY 2018/19 auction as an important stage for determining a streamlined approach that ensure the qualification workload on the RAs and market participants is manageable.

4.2 CY Parameters

Q. Do you agree with the SEM Committee's minded to position to keep the parameters (excluding capacity requirement and de-rating factors) for the CY2019/20 capacity auction consistent with the CY2018/19 parameters?

A. ESB GWM do not agree with the SEM Committee's minded to position to not review the APC, ECPC and USPC in advance of the T-4 auction. The level of detail and consultation for the first transitional capacity auction CY 2018/19 should not conclude in the removal of the requirement to review/change the CY 2019/20 and CY 2020/21 auction parameters.

Considering the tight auction timelines and the methodology used to determine the initial APC, ESB GWM consider it prudent and efficient to apply the same methodology to yearly deviations in the CRM auction parameters i.e. the automatic application of an inflation component.

As per section 3.1.1 of this response, ESB GWM suggest a review of the 0.5 multiplier prior to the next auction.

4.3 De-Rating Factors

Q. Do you agree with the proposed modification to the treatment of outages for small and embedded capacity in GB in the interconnector de-rating methodology?

A. For the interim "interconnector led" solution, ESB GWM consider the proposed modification to the treatment of outages for small and embedded capacity in GB as appropriate. A change to the cross border participation from the interim "interconnector led" to the enduring "hybrid" approach may require a review of assumptions.

Q. Do you agree with the use of a least-worst regrets approach to the choice of GB generation scenario used to set EMDF?

A. ESB GWM consider the application of the same process to GB based participants as proportionate since the least-worst regrets approach is applied to I-SEM based participants.

Q. Do you agree with the approach that the EMDF need only be determined for the GB market for CY2019/20 in the absence of interconnection with other markets?

A. ESB GWM suggest that the EMDF approach should be reviewed on an auction basis taking into account the potential implications GB's interconnection with other markets may have on the de-rating factor used for the current methodology.

4.4 **Appendix: De-Rating Factor Calculation Methodology**

Q. Do participants have any comments on the methodology for calculating DRFs for storage units as described in this paper?

A. In principle ESB GWM agree with the new methodology.

Q. In the absence of significant historical data, do participants consider it reasonable to apply system-wide outage statistics to new technologies (such as batteries)? If not, please provide alternative with justification.

A. ESB GWM agree with the proposal to apply system-wide outage statistics to new technologies in the absence of I-SEM or international data.

Q. Regarding Storage Units with Storage Volume sizes that are not a multiple of 30 minutes: Do participants have any comments on the TSO's preferred methodology for calculating DRFs for such storage units, i.e. interpolating between storage sizes? What other options do they believe may be more appropriate?

A. ESB GWM agree with the proposed linear interpolation between storage sizes.

Q. Should storage units be allowed to apply a DECTOL to their De-rated Capacity? Please provide arguments to support your response.

A. Yes but at the unit's discretion. ESB GWM request further information on the requirements that need to be provided to demonstrate the storage capability.

Q. Should specific DRF values be published for units with energy storage volumes of 6.5 hours or greater? Are participants aware of potential projects that might make such a change appropriate?

A. ESB GWM are unaware of any storage unit that would require greater than 6.5 hours. ESB GWM would suggest that application of the 6.5 de-rating factor to apply to any unit that did require greater than 6.5 hours until a review could be performed.

Q. Do participants consider that a unit's run-hour limitations (due to emission restrictions or otherwise) should be reflected in the Capacity Market Auction? If so, what mechanisms should be applied. If not, please provide rationale.

A. ESB GWM believe the significance of this proposal warrants an individual consultation. The detail provided in this consultation is not at a level for ESB GWM to comment on the mechanism. ESB GWM are of the view that greater detail on the proposal and potential impacts must be consulted upon prior to any decision. ESB GWM believe to introduce such a proposal for the CY 2019/20 auction would not be providing this proposed mechanism with the due diligence and regulatory attention that it requires.

Due to the lack of detail surrounding the proposal, ESB GWM do not agree with this mechanism. ESB GWM consider it is for the contract holder to ensure they fulfil their contract obligations. Therefore, the commercial risk for the holder should be managed by the holder (possibly via a voluntary DECTOL or a fully functioning secondary market) and not enforced through extra regulatory intervention (mandatory DECTOL). ESB GWM suggest if the DECTOL is being reviewed for run-hour limited unit it may also be beneficial to review the SEMC decision on the DECTOL for all market participants.

To conclude, ESB GWM request a specific consultation to address if there is a need for any potential mechanism for run-hour limited units and identify the consequences of potential mechanisms

Q. Do participants have any comments on the proposed approach for de-rating DSUs with limited Maximum Down Time?

A. ESB GWM agree with the proposed approach that treat all storage units in an equitable manner.

4.5 Long Stop Date

Q. Do you agree with our revised proposals for Long Stop Dates and Substantial Financial Completion dates as set out in the section, and summarised in Table 4.

A. ESB GWM agree with the revised proposals for the Long Stop dates and Substantial Financial Completion dates.