Single Electricity Market (SEM)

Supplementary Consultation Paper on modified and combined Modifications to Facilitate Delivery of Capacity

SEM-23-080

6 October 2023

Contents

1. Background

There have been a number of proposed CMC modifications raised in 2022 and 2023 which relate to difficulties which CRM auction winners are facing in meeting key deadlines, such as meeting the Substantial Financial Completion (SFC) Date or the Long Stop Date. In addition, other CMC or TSC modifications have sought to address the impact of delays on financial viability, including indexation proposals and proposals aimed at reducing the potential impact of contract erosion.

Contract erosion occurs where a market participant with a Reliability Option contract fails to achieve Minimum Completion by 1 October of the first contract year, leading to a shortening of the period for which capacity payments are made[1]. This effect provides a key financial incentive for capacity developers to deliver their projects on time and is commonly seen in capacity contracts in other jurisdictions. However, in certain circumstances, reducing contract erosion could lead to significant consumer benefits if it prevents investors from terminating projects, with the result that they complete their projects. This will lead to a material improvement in security of supply and/or reduced need for costly emergency interventions, such as Temporary Emergency Generation.

The SEM Committee have approved a modification containing elements of some of the CMC modifications raised to mitigate the impact of delays on projects, specifically:

- In SEM-23-001, the SEM Committee required that the SOs implement the modification set out in Appendix B of that document which combined elements of the proposals CMC_12_22, CMC_13_22 and CMC_15_22. The combined modification set out in SEM-23-001 provided for the SOs to extend the SFC and Long-Stop Date for a Capacity Market Unit (CMU), where that CMU had been subject to a Third-Party Judicial Review or Third-Party Planning Appeal. The SFC and Long Stop Date can be extended by a period equal to the Third-Party

[1] Suppose, for instance, an investor had won a contract for 10 years in the 2024/25 T-3 auction, at €140/kW$_d$/year for 10 years. Suppose that the investor fails to achieve Substantial Completion by 1 October 2024, but achieves Substantial Completion on 1 January 2026, i.e., 15 months after the start of the first delivery year. Unless the Capacity Quantity End Date and Time are extended by 15 months, the investor will receive the CRM payment of €140/kW$_d$/year for 8 years and 9 months, rather than for the full 10 years. It is worth noting the investor may be able to enter into an auction for 2034/35 and subsequent years but they will have face 15-months contract erosion at the original contract price..

Extension Period where that Capacity Market Unit is subject to a Third-Party Judicial Review or Third-Party Planning Appeal. Whilst the Third-Party Extension Period is not explicitly limited, the SOs may propose to the Regulatory Authorities the termination of the Awarded New Capacity for which an extension was granted if the Capacity Market Unit (CMU) does not achieve the SFC within 18 months of the original SFC Date. The participant may also seek the approval of the RAs to extend the Capacity Quantity End Date and Time by a period no greater than the Third-Party Extension Period, to mitigate the impact of contract erosion. Subsequent modification proposals from industry sought to address additional flexibility around planning concerns and contract erosion as follows:

- CMC_11_23 proposed that if a planning application is "called-in" under Article 17/18 of the Planning Order (NI) this should be treated similarly to a Third-Party Judicial Review or Third-Party Planning Appeal, under the approved above modification.
- CMC_13_23 proposed to allow a unit to achieve Minimum Completion (60% of awarded capacity), without having to wait until the LSD date, if it does not achieve the Minimum Substantial Completion level of 90% of awarded capacity. This modification could enable some capacity units to get paid up to 18 months earlier, preventing up to 18 months of contract erosion.

There have been a number of other proposed modifications which relate to other causes of delay potentially faced by the winners in recent auctions, such as delays in the delivery of grid and/or gas connections or extraordinary supply chain events as follows:

- CMC_04_23: Introduction of remedial action for unforeseeable delays due to extraordinary supply chain impacts, which the RAs propose to be modified and combined with other mods as presented in this consultation

- CMC_10_23: Mitigation of Impact on Participants relating to 3rd Party Gas Connection delays, which the RAs propose to be modified and combined with other mods as presented in this consultation

- CMC_23_23: Mitigation of Impact on Participants relating to System Operator Grid Connection delays, which the RAs propose to be modified and combined with other mods as presented in this consultation

The SEM Committee recognises that Capacity Market Units which have been successful in recent auctions face a variety of significant challenges in delivering contracted capacity. Many of these challenges result from the sheer scale of capacity that the SEM is seeking to connect in order to transition to the low carbon economy, whilst meeting growing demand at the same time. The SEM has already contracted over 3,600MW_d of pre-dominantly gas-fired multi-year New Capacity[2] at the same time as seeking to connect over 8,000MW of new renewables capacity between 2023 and 2030[3]. This unprecedented level of new connections is imposing or is likely to impose a strain on a number of institutions, including environmental permitting agencies, electricity TSOs and gas grid operators.

Some delays are likely to be within the control of market participants, and there may be cases where market participants' own actions, or events which market participants may reasonably have anticipated and/or mitigated, have contributed to delays. However, it may also be the case that there are other delays which are at least partially caused by other key institutions on the island of Ireland or in the wider economy, which market participants may not have reasonably anticipated, and which they can do little to mitigate.

The recent EY report recommended that the SEM Committee take a more permissive approach to requests for extensions, from new build projects, and the SEM Committee committed to consider adopting a more permissive approach on a case-by-case basis (see SEM-22-054).

In the current security of supply circumstances, there may be benefit to consumers in implementing some additional, potentially time-limited, modifications to the CMC/TSC, which do more to address some of the challenges faced by investors in delivering capacity under the current circumstances. The key benefit to consumers is avoiding

[2] Net of terminations

[3] Based on the 2022 Generation Capacity Statement

lost load and/or the need for costly emergency measures, such as Temporary Emergency Generation.

The SEM Committee has considered the outstanding CMC Modification Proposals. Whilst, in line with the EY report recommendations, it recognises that there may be merit in a more permissive approach to handling delays, it considers that there are a number of flaws in the outstanding proposals. Generally, the Modifications proposed by market participants:

- Are a series of piece-meal attempts to address a series of different root causes, in response to particular circumstances faced by projects. They do not provide a holistic solution, and market participants' current approach could lead to a series of urgent proposals which are "ad-hoc" responses to individual events;
- Tend to be open ended, and do not facilitate distinction between delays, where market participants may never contribute to resolving the capacity gap in the mid-2020s, and projects which could contribute to resolving the gap, with a more permissive approach;
- Do not do enough to distinguish between delays which are outside the control of market participants, and those which could not reasonably have been anticipated or mitigated by market participants.

The SEM Committee is of the view that the current "ad-hoc" approach of proposing individual Modifications which seek to define *ex ante* the types of events which would merit automatic extensions of the SFC Date and/or Long-Stop Date will not appropriately address the issues and will not optimally deliver CMC objectives.

Rather than approving a series of CMC/TSC Modifications which seek to define ex ante the circumstances which will lead to the grant of extensions, the SEM Committee is considering implementing more generalised provisions in the CMC which will include provisions for the SEM Committee to grant extensions on a case-by-case basis, as and when market participants apply for extensions to the Substantial Financial Completion date, the Long-Stop Date, and the Capacity Quantity End Date and Time. Such extensions will be granted only where the grant of the extension is consistent with the CMC Objectives as specified in Section A1.2 of the CMC, when the market participant has justified the request with robust evidence, and where the extension would otherwise be consistent with the SEM Committee's statutory duties.

2. SEM Committee proposals

Rather than approving proposals CMC_01_23, CMC_04_23, CMC_09_23, CMC_10_23, CMC_16_23, or CMC_23_23 related to delays currently before the SEM Committee for approval as written, the SEM Committee is considering using its powers under B.12.11.4 of the CMC[4] to make two different modified and combined Modifications which have an increased scope and may be more appropriate to the current situation.

The SEM Committee is considering the following modified and combined modifications (as explained in Section 2.1 and Section 2.2):

- **Linking approval of Substantial Financial Completion Delays to Long Stop Dates and Capacity End Date and Time for specific auctions**
- **Providing a mechanism for the SEM Committee to approve extensions to the Long Stop Date and Capacity Quantity End Date and Time for specific auctions**

The first aims to reduce the risk to investors that a new CMU can meet its extended SFC Date, but decides to terminate rather than proceed to SFC because either the developer:

a) cannot deliver in time to meet the original Long Stop Date, because of delays in achieving SFC; or

b) can still meet the Long Stop Date, but the impact of contract erosion means that the project is no longer financially viable.

[4] B.12.11.4 of the CMC states that, "B.12.11.4 The Regulatory Authorities may make a Modification that is different (including one that is materially different) from that proposed in a Modification Proposal, Workshop or consultation notice if the Regulatory Authorities are satisfied that, having regard to the issue or issues that were raised by the Modification Proposal, that the different Modification will or is likely to better contribute to the achievement of the Capacity Market Code Objectives".

The second aims to mitigate risks that materialise after SFC has been achieved. For instance, suppose that an investor is in a position to achieve SFC by the original SFC Date, so has no need to apply for an extension. Assume the investor is offered a connection agreement with an expected connection date which would allow it to meet the Long Stop Date. However, the investor still faces risks that if it proceeds to sign contracts, the connection is late in being delivered, with the result that either:

a) The new CMU fails to meet the Long Stop Date; or

b) The delay in achieving completion is such that contract erosion occurs to such an extent that proceeding with the project is no longer financially viable

This modification aims to mitigate risks that appear post-SFC, by providing a mechanism for investors to apply to the RAs to obtain extensions to the Long Stop Date and the Capacity Quantity End Date and Time, even after SFC is achieved.

2.1 Linking approval of Substantial Financial Completion Delays to Long Stop Dates and Capacity Quantity End Date and Time for specific auctions

Under this proposal the SEM Committee is considering implementing a Modification which links extensions in the Substantial Financial Completion Date to extensions in the Long-Stop Date and Capacity Quantity End Date and Time.

A unit that is successful in a T-3 or T-4 auction has to achieve SFC within 18 months of the Auction Date. If it considers that it will fail to meet that deadline, and it wishes to extend that deadline, it is required to submit a request to the SEM Committee to extend the SFC deadline at least 20 Working Days in advance of the SFC deadline, in accordance with J.5.2.5 of the CMC. The SEM Committee has the discretion to extend the SFC deadline.

However, in granting an SFC extension, the investor is still bound by the same LSD and Capacity Quantity End Date and Time as before, unless it specifically meets the circumstances set out in the decision published in SEM-23-001[5]. Therefore, unless it is

[5] including the specific circumstances provided for in CMC_11_23, which includes “calling-in” of a planning decision under Article 17/18 of the Northern Ireland Planning Code

subject to a Third-Party Judicial Review or Third-Party Planning Appeal, even if New Capacity is granted the SFC extension, the grant of the SFC extension will not mitigate any risks of the delay causing it to miss the LSD, or of contract erosion. Therefore, for instance, if the delay is due to a backlog in New Capacity seeking environmental permits, if the SEM Committee extends the SFC deadline, there is no automatic extension in the LSD and the New Capacity will still be expected to bear contract erosion.

Meeting the LSD may be challenging, particularly for T-3 auction winners, who had circa 2 years 6 months to build capacity following contract award.

This modification will ensure that where the SEM Committee considers that an SFC extension is appropriate in light of CMC Objectives and the SEM Committee uses its powers to grant an SFC extension to multi-year New Capacity, there will be a mechanism within the CMC for the SEM Committee to consider a commensurate extension to the LSD and to the Capacity Quantity End Date and Time, should this be sought.

The SEM Committee is considering whether to restrict these provisions to specific auctions. The automated extensions could apply only to the 2024/25 T-3 and 2025/26 T-4 auctions, i.e., the auctions to which the indexation provisions as per SEM-23-038 apply. However, whilst indexation was restricted to those who were successful in these auctions on the basis that these investors were most likely to have faced unanticipated inflation, it could be argued that whilst inflation risk may have subsequently reduced, delay risk applies to winners in a wider set of auctions. Difficulties in obtaining timely planning and permission remains and difficulties in obtaining timely electricity and gas grid connections may be intensifying as Ireland and Northern Ireland seek to build and connect unprecedented levels of new renewables and gas-fired capacity. This may suggest that if this modification applies to specific auctions, the provisions should apply to multi-year New Capacity winners of all T-3 and T-4 auctions held to date, up to and including the 2027/28 T-4 auction.

In considering the CMC Objectives, it is legitimate for the SEM Committee to reflect security of supply circumstances at different times, and for instance, apply a more permissive approach to granting extensions at times when there is a capacity shortage, than at times when there is surplus capacity. However, it may be argued that if this modification was introduced into the CMC for an unlimited period, the SEM Committee would be encouraging investors which are at greater risk of delay to seek qualification or could have moral hazard effects such as limiting the incentive on investors to choose locations where they are more likely to get permissions and connections quickly. In any event, a time limited “sunset” approach would enable the SEM Committee to review the operation of the modifications before deciding whether to introduce them on a longer-term basis.

The SEM Committee is aware that if this Modification is implemented, it will not be implemented in time for any New Capacity awarded in the 2024/25 T-3 auction to apply for an extension to the Long Stop Date and the Capacity Quantity End Date and Time, at the same time as an SFC Date extension. The SFC deadline for the 2024/25 T-3 auction was 4 September 2023, and extension applications were due 20 working days in advance of the SFC deadline. Additionally, the SFC deadline for New Capacity awarded in the 2025/26 T-4 auction is in November 2023, and it is unlikely that this Modification will be implemented before the deadline for SFC Date extension applications for the 2025/26 T-4 auction either. Therefore, the SEM Committee is considering implementing provisions which would allow New Capacity which has been granted SFC extensions prior to the implementation of this Modification, but have not yet met SFC, to apply to the RAS for extensions to their Long Stop Dates and Capacity Quantity End Date.

2.2 To provide a mechanism for the SEM Committee to approve extensions to the Long Stop Date and Capacity Quantity End Date and Time for specific auctions

The SEM Committee are also considering the merits of introducing a second modification to provide a mechanism where a market participant with a multi-year New Capacity contract can apply for an extension to the Long Stop Date and/or the Capacity Quantity End Date and Time, at any point up until 20 Working Days before the Long Stop Date.

Under this modification, where a CMU is awarded a multi-year Reliability Option now expects completion to be delayed so that it will either miss its Long Stop Date and/or suffer contract erosion, it may apply to the SEM Committee to extend the Long Stop Date and/or the Capacity Quantity End Date and Time.

The applicant must specify the reason(s) for the delay, and new projected dates for completion. The applicant must supply any further information that the SEM Committee deems appropriate to assist it in making that decision, and will require evidence of delays, including documents from third parties such as suppliers.

The SEM Committee may choose to extend either the Long Stop Date and/or the Capacity Quantity End Date and Time, where it judges that such an extension is consistent with the CMC Objectives.

That means, that if there are delays in delivering capacity which occur after SFC but before completion (e.g., due to delays in delivering connections after connection agreements are signed), the risk to the CMU of missing the Long Stop Date or of contract erosion are mitigated. Furthermore, if at the time of requesting an extension to SFC, if the market participant is aware of reasons why the delay to achieving completion is likely to be longer than the delay to SFC, it can reflect it in its application for extensions to the Long Stop Date and Capacity Quantity End Date and Time.

The SEM Committee may choose to set a time limit for the extension to the Long Stop Date and the Capacity Quantity End Date and Time, which is shorter than requested by the applicant. If the relevant CMU achieves completion before the revised deadlines, the maximum period for which it can be paid for capacity will be ten years, or the length of the originally awarded contract, whichever is shorter.

The intent of this proposal is to ensure that where a market participant is in a position to sign contracts and achieve SFC, it can do so, knowing that if there are subsequent delays which are beyond its reasonable control there is a mechanism available for the SEM Committee to mitigate its risk, in justifiable circumstances. However, seeking extensions should not be the default approach for investors, and investors should not assume that they can seek to qualify enter high-risk projects, and subsequently seek extensions to mitigate these risks. This Modification proposal is not intended to completely remove delivery risk from the investor – if delays are extensive and are such that other solutions are likely to better achieve CMC Objectives (such as deliver capacity earlier), extensions may be limited.

This may apply to multi-year New Capacity in T-3 and T-4 auctions held to date, inclusive of the 2027/28 T-4 auction.

3. Consultation Questions

The SEM Committee welcomes views and responses on the proposed modifications raised within this consultation paper.

Respondents are invited to provide comments and feedback on the proposed Modifications in respect of:

- the proposed modifications and their consistency with the CMC Objectives;
- any impacts not identified in the Modification Proposal Forms, e.g., to the Agreed Procedures, the Trading and Settlement Code, Grid Code, testing and outages, and IT systems etc.; and
- the detailed CMC drafting proposed to deliver the Modifications.

4. Next Steps

The SEM Committee are seeking views from industry on both proposals, and intend to make a decision in November 2023 on implementing one or both of the Modifications as outlined within this consultation paper.

Responses to the consultation paper must be sent to both the CRU and UR CRM Submissions inboxes by no later than 17:00 on October 20th 2023.

CRMsubmissions@uregni.gov.uk

CRMsubmissions@cru.ie

Please note that late submissions will not be accepted.

Please note that we intend to publish all responses unless marked confidential. While respondents may wish to identify some aspects of their responses as confidential, we request that non-confidential versions are also provided, or that the confidential information is provided in a separate annex. Please note that both Regulatory Authorities are subject to Freedom of Information legislation.