



Energy for
generations



T-3 2027/2028 CAPACITY AUCTION PARAMETERS

SEM Committee Consultation SEM-24-012

ESB GT Response

23rd February 2024



Contents

Introduction.....	3
Responses to proposals in relation to Auction Parameters	3
ESB GT Proposals	4
Conclusions	6

Introduction

ESB GT welcomes the opportunity to respond to the SEM Committee (SEMC) on this consultation paper (**the Consultation**) relating to the SEMC's proposals to change the relevant parameters to apply in the 2027/2028 T-3 Capacity Auction, scheduled to take place on 26th September 2024.

Before responding to the specific proposals within the Consultation, ESB GT wishes to state that it believes that the holding of a T-3 Auction may potentially undermine future Capacity Remuneration Mechanism (CRM) auctions by sending conflicting signals to potential investors, thus undermining confidence in the ability of the CRM to deliver security of supply at lowest cost to consumers.

The announcement of a T-3 for 2027/28 has **delayed the holding of a T-4 auction for 2028/29** which had been due to take place in September/October 2023. This announcement comes **less than 3 months** after the publication of the *SEM-23-036 Consultation Response Document - EY Review of the Performance of the SEM CRM*¹, wherein **the following commitment was made** in response to the EY recommendation (which was itself based on industry feedback) that:

*“The SEM Committee, along with the TSOs **will seek to allow a minimum of the full 4 years of lead time for new builds in subsequent T-4 auctions for the foreseeable future. To expediate the process, the SEM Committee will consider faster approval of Final Capacity Auction Results.**”*

ESB GT believes that rather than holding a T-3, the T-4 auction for 2028/29 should be brought forward and, as repeatedly requested by industry, including at the Senior Stakeholder Forum held in respect of this T-3 Auction process, that the SEMC should move towards T-5 or even T-6 auctions and enhance the reward for any unit delivering early. Such incentives should address the T-3 auction objective.

Responses to proposals in relation to Auction Parameters

ESB GT does not support the proposed changes to the Capacity Auction Parameters as outlined in the Consultation as they do not address the fundamental issues affecting the delivery of new capacity, as highlighted in the *‘EY Review of the Performance of the SEM CRM’*² commissioned by SEMC which included such recommendations as:

- *“Ensuring 4 years lead time for T-4 Capacity Auctions”.*
- *“A Recalculation of the reliability standard”;* and
- *“A Requirement for new prospective capacity to have all the necessary consents to prequalify for an auction.”*

The fact that the substantive proposals in the Consultation (increase in APC and non-zero INCTOL) appear to be targeted solely at this T-3 Auction, and are therefore potentially temporary in nature, will only serve to target the symptoms of the issues facing the CRM and not the causes of the continued lack of delivery of sufficient new capacity.

¹ [SEM-23~1.PDF \(semcommittee.com\)](#) – pg. 3

² [SEM-23~1.PDF \(semcommittee.com\)](#) – Table 1 and Table 2

Recent modifications to permit extensions to specific dates in capacity contracts that have been approved by the SEMC, have resulted in the cliff edge risks in relation to project delivery being reduced.

It is therefore also important that given the very short lead time of this new auction (and given the evidence of the need for increased time to address unforeseen blockages such as planning, grid connection etc), that the proposal itself along with the modifications does not introduce moral hazard and in turn undermine the objective of this earlier T-3 auction.

Additionally, an effective increase in De-Rating Factors (DRFs) **may not fundamentally introduce any physical new capacity** into the system which will do nothing to improve actual system reliability issues but may allow parties to rebalance their risk appetite.

If it is decided by SEMC to move forward with allowing a non-zero INCTOL, as a matter of equity, the **proposed INCTOL provision should be available to all Existing Capacity** differentiated by technology (e.g., Storage Units, DSUs etc). This will allow units with historically higher availabilities to take on a larger capacity obligation, with the potential to maximise participation and introduce some effective competition to the auction.

Notwithstanding the above, ESB GT does not believe that the Consultation proposal serves in the best interest of the consumer, and potentially only dampens investor confidence in the CRM, particularly considering the delay to the holding of the T-4 auction. It is key that confidence is maintained by the SEMC committing to the appropriate timelines and sending the right consistent signals to participants.

ESB GT believes that if changes are to be implemented by the SEMC that these should be enduring to ensure that stable incentives are in place to deliver new capacity as opposed to having parameters and methodologies changing on a regular and uncertain basis, which will only introduce regulatory uncertainty and with it, additional risks and related costs.

To support the SEMC in its objective of delivering assets onto the system at an earlier date than the timetabled T-4, ESB GT puts forward the following proposed changes to Auction Parameters and policy, which should be an enduring part of all future auctions. ESB GT hopes that these proposals will be considered and that they can be seen to deliver the ultimate objective.

ESB GT Proposals

1. **Increase the APC** to a level that appropriately reflects the real-world development costs and risks faced by project developers.

In 2016, at the outset of the SEM design phase, SEMC³ *“noted that most other capacity auctions have Auction Price Caps, typically set in the range 1.5 to 2 x Net Cost of New Entrant (Net CONE)”*.

All auctions to date have used a multiplier of 1.5.

Setting an appropriate APC that will endure will encourage competition, including incentivising new participants to bring forward projects that can be ‘bankable’ and deliverable at an appropriate, competitive rate of return. It will also contribute somewhat to lessening the impact

³ [SEM-16-039 CRM Decision 3 \(Updated pg\).pdf \(semcommittee.com\)](#)

of having ex-ante price caps in a market and may incentivise wider participation by supporting the lessening of the winner’s curse. In addition, a fundamental review of the Best New Entrant pricing methodology should be undertaken to ensure it is still fit for purpose in terms of enabling security of supply and incentivising low carbon generation to meet national climate targets.

2. Increase the Existing Capacity Price Cap (ECPC)

The auctions should send appropriate and equal investment signals to existing operators that capacity is valued in what will continue to be a situation of scarcity in the dispatchable generation sector for many years to come. Operators must be incentivised to invest in the operation, maintenance, and refurbishment of assets to provide system security and resilience. This will ensure sufficient competition to maintain downward pressure on the auction clearing price for existing capacity but will also reward these existing units effectively allowing them to reinvest in their units and deliver within much shorter timelines than new units. ESB GT is aware of additional limitations imposed on some units through the Industrial Emissions Directive, but still believes that this approach can deliver on security of supply requirements faster and more effectively.

3. Ongoing Transparency on capacity requirements is necessary.

It remains unclear to industry how the capacity deficits outlined in successive Generation Capacity Statements are translated into the demand curve used in each auction. This fact was called out in the EY Report.

“the SEMC are in the process of establishing a panel of technical experts to increase transparency and provide independent advice to the SEMC on its volume setting process for auctions”.

The SEMC published an ex-post 2026/27 T-4 Auction, Volumes Information Note in November 2023. It is important that such analysis and justification of forecast volume procurement is conducted in advance of all future auctions and that the assumptions are updated on a regular basis to reflect grid development works and any changes in overall energy policy likely to impact on capacity requirements.⁴ Relevant points made by the SEMC in the information note which highlight the issues from an industry perspective include:

“The EY report highlights the fact that there is limited transparency in how the TSOs’ demand forecasts are translated into the key volume parameters for the auction, including how the TSOs calculate their adjustments, and why the SEM Committee decides to accept some of the adjustment recommendations, but not others.”

...

“For instance, at the time the TSOs were making their recommendations on adjustments, they had no visibility of the decisions that the SEM Committee was going to make with regard to indexation of contracts awarded in the 2024/25 T-3 auction, and the 2025/26 T-4 auction, and to what extent the policy intervention will mitigate risks.”

...

⁴ [CRM 26 27 T-4 Auction Volumes Information Note.pdf \(semcommittee.com\)](#) – Section 2

“The SEM Committee has taken a balanced approach when approving adjustments to CRM auction volumes. On the one hand, if adjustments are too conservative, they run the risk of further increasing consumers’ capacity bills. On the other hand, the SEM Committee is also aware that if a higher-than-expected number of risks materialise, then the cost / MWd / year of remedial actions could be significantly greater than the cost of procuring more capacity via T-4 auctions.”

In their response⁵ to the consultation on the EY Report, the TSOs made the following statement:

“Such decisions have consistently failed to provide supporting argument as to why EirGrid and SONI recommendations for new generation capacity have been apparently arbitrarily discounted and where no factoring has been included to take account of the inevitable attrition which will ensue for development projects of this nature.”

Given the views expressed above by both SEMC and the TSOs, it is important that SEMC reasoning for adjustments to TSO recommendations is made clear to all market participants, and that the criteria applied are transparent and consistent for each auction going forward.

4. Introduce Unit based derating factors (DRFs)

The SEMC acknowledges in the Consultation that older, less reliable units are impacting on the derating applied across the general technology classes participating in the capacity market.

A full operational history is available for all existing units which, when combined with forward looking asset management and maintenance, could be used to justify unit specific DRFs or requests for non-zero INCTOL parameters.

In seeking increased (or decreased) unit specific DRFs or INCTOL/DECTOL, market participants are in a position to manage the appropriate level of risk they assume in relation to the Reliability Option they are seeking to hold for each of their units.

This differentiated approach will incentivise competition as more reliable units within technology classes will be more viable than less reliable ones.

In conjunction with introducing changes to DRFs, SEMC should ensure that the capability to appropriately trade capacity on the secondary market is facilitated to allow market participants to appropriately manage their exposure risk of holding Reliability Options. Such arrangements have been awaited in the CRM for a considerable length of time.

Conclusions

ESB GT believes that it is important that SEMC focuses its efforts on fundamental enhancement to the CRM rather than ‘piece-meal’ interventions in reaction to the failures of previous auctions.

ESB GT does not believe that a T-3 auction is in the best interest of the overall system and consumers in the long term.

⁵ [EirGrid & SONI response to SEM-22-054.pdf \(semcommittee.com\)](#) – pg.4

ESB GT believes that the SEMC and the TSOs should focus their efforts on holding the next T-4 auction as soon as possible, including fundamental reforms which deliver the appropriate incentives to ensure maximum participation by project developers, and with the potential for bonus incentives for the early delivery of successful projects.

ESB GT would welcome engagement on a bi-lateral basis with both the SEMC and the TSOs, in addition to as part of a wider industry consultative process in relation to enhancements to the capacity auction process.