

SEM Balancing Market and Capacity Market Options

SEM Committee Consultation

SEM-19-024

Power NI Response

11 July 2019

Introduction and General Comment

Power NI welcomes the opportunity to respond to the SEM Committee's consultation entitled Balancing Market and Capacity Market Options. The SEM Committee position this paper as being in response to concerns over the performance of the Balancing Market following the implementation of the amended energy trading arrangements on 1st October 2018. Power NI recognises and is equally concerned by the Balancing Market outcomes and in particular the performance of central market systems since the 1st October 2018. Power NI considers the central market systems and therefore the Balancing Market more broadly, as not yet in a stable state. This instability and uncertainty is a key influencing factor in Power NI's consideration of the SEM Committee proposals particularly in relation to Option 1 – 'Simple NIV tagging'.

In reviewing the SEM Committee proposal Power NI firstly considers if the change is a fundamental design amendment, consistent with the High Level Design and secondly does sufficient and robust evidence exist to support the change?

The Balancing Market pricing methodology was considered at length during the High Level and Detailed Design Phase of the ISEM Market Project. A significant amount of time was devoted to the topic at the Detailed Design Workshops and the methodology was included in a number of consultations, most notably SEM-15-026, Energy Trading Arrangements Detailed Design, Markets Consultation Paper in June 2015. The conclusion reached by the SEM Committee following this piece of work was that the 'flagging and tagging' approach should be adopted and while it acknowledged that the simple approach could be retained as a backup the disjoin from actual balancing actions and lack of true cost reflectivity were cited as reasons for not adopting that approach from the outset.

Set against that context Power NI does consider the proposal under Option 1 'Simple NIV tagging' to be a fundamental change and is somewhat surprised that the SEM Committee would move straight to a 'minded to position' on this approach without the rigour of industry engagement via Balancing Market pricing workshops, consultation and then a 'minded to' position. Power NI would naturally be concerned that this proposal has been rushed through without the necessary due diligence to support such a significant change.

The SEM Committee appear via the Consultation Paper to justify the minded to position approach by implying that expedience is necessary. Power NI would strongly prefer broad industry engagement on the topic as the proposal is a fundamental change and raises policy questions in relation to cost reflectivity, marginal pricing, simple versus complex price comparisons and the impact on imperfections charges. If however the SEM Committee are convinced that expediency is necessary then it places an even greater emphasis and need for robust evidence to support the decision. It is in this area where Power NI's primary concerns lie.

As the SEM Committee is aware there have been a significant number of Balancing Market pricing defects witnessed in the Central Market Systems since go-live on 01 October. Such are the magnitude of the defects encountered practically every day from 01 October 2018 to mid-June 2019 have been subject to upheld pricing disputes and under the Trading and Settlement Code should be re-priced. This means that the true Balancing Market prices for that period are not yet known and any analysis performed on the currently published prices are subject to change, perhaps materially. In addition the market has only been running for a relatively short period of time and not yet completed a full annual cycle, and while there have been two extreme events consideration must be given if they are sufficient justification for making the change and thirdly a significant modification (MOD_09_19) was approved by the SEM Committee in May 2019 which has impacted the Balancing Market price effectively re-baselining any analysis. In reality therefore the only Balancing Market prices which can be relied upon are those post the June 2019 software update that corrected outstanding material defects that had given rise to the manifest pricing errors. This analysis only considers data covering the first five months of market operation, which is itself a small unrepresentative window, covering winter months that were also impacted by a number of coincident generator outages, and where the pricing was materially incorrect. This extremely limited and error riven data set is not a sound foundation upon which to base such a fundamental decision. This is of real concern to Power NI.

In relation to Option 2 and the impact on the Capacity Market, Power NI has considered this issue from its perspective as a supplier who operates without a Reliability Option and values the protection provided by the Socialisation Fund.

Specific Questions

The SEM Committee posed a number of specific questions within the Consultation Paper and Power NI has sought to deal with each in turn.

Consultation Question 2.1: Do you support this Simple NIV tagging option and its implementation in the SEM?

Power NI response:

Power NI does not feel in a position to fully answer this question at this time. This position should not be interpreted as Power NI abdicating its responsibilities as a participant but rather a reflection of the lack of evidence available upon which to base a view.

As stated above there has been a significant number of material Balancing Market pricing defects witnessed in the Central Market Systems since go-live on 01 October.

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In addition to the unreliable Balancing Market pricing evidence, Power NI, as a supplier, is concerned by the lack of information in relation to the impact on the imperfections charge. This charge is potentially increasing by 99% per SEM Consultation Paper SEM-19-031, significantly increasing the cost to consumers.

Consultation Question 2.2) Do you have any concerns regarding moving to Simple NIV tagging in the Balancing Market, including the risk of unintended consequences? If so, please explain these concerns.

Power NI response:

The lack of a robust evidence set makes it difficult to identify the actual consequences never mind any unintended consequences. From a supplier and customer perspective Power NI would be concerned about the impact on imperfections charges and would urge the SEM Committee to consider this direct charge to consumers in their analysis and impact assessment.

Power NI also recognises that a simple stack will be priced on both simple and complex bids. Will this cause an issue also requiring remedy such as uplift? If this is the case this also needs to be fully understood. If a mixture of simple and complex prices does depress BM prices relative to the ex-ante markets then that could create commercial incentives that conflict with the obligation for participants to be balance responsible. Any such potential for distortion to the overall market efficiency across all the energy markets would also need to be considered.

Consultation Question 2.3) Do you agree or disagree that Simple NIV tagging meets the I-SEM High Level Design, the I-SEM Detailed Design and the I-SEM market power mitigation decision? If you disagree, please explain why.

Power NI response:

As stated above the Balancing Market pricing methodology was considered at length during the High Level and Detailed Design Phase of the ISEM Market Project. A significant amount of time was devoted to the topic at the Detailed Design Workshops and the methodology was included in a number of consultations, most notably SEM-15-026, Energy Trading Arrangements Detailed Design, Markets Consultation Paper in June 2015. The conclusion reached by the SEM Committee following this piece of work was that the 'flagging and tagging' approach should be adopted and while it acknowledged that the simple approach could be retained as a backup the disjoin from actual balancing actions and lack of true cost reflectivity were cited as reasons for not adopting that approach from the outset. Power NI therefore believes that the change proposed represents a material/significant change in the ISEM design decisions.

At a principle level however inconsistency with previous decisions should not preclude changing something which is fundamentally flawed if the change has been subject to extensive industry consultation and is supported by a robust suite of evidence. However, that is not the case with the evidence presented in the consultation paper.

Consultation Question 2.4) Do you agree or disagree with SEM Committee's assessment that the pricing outcomes under Simple NIV tagging are preferable, given market fundamentals? If you disagree, please explain why.

Power NI response:

As stated above there has been a significant number of Balancing Market pricing defects witnessed in the Central Market Systems since go-live on 01 October. Such are the magnitude of the defects encountered practically every day from 01 October 2018 to mid-June 2019 have been subject to upheld pricing disputes and under the Trading and Settlement Code should be re-priced. This means that the actual correct Balancing Market prices for that period are not yet known and any analysis performed on the currently published prices that are known to be incorrect has a high probability of being flawed. In reality therefore the only Balancing Market prices which can be relied upon are those post the June 2019 software update that corrected outstanding material defects that had given rise to the manifest pricing errors. This analysis only considers data covering the first five months of market operation, which is itself a small unrepresentative window, covering winter months that were also impacted by a number of coincident generator outages, and where the pricing was materially incorrect. This extremely limited and error riven data set is not a sound foundation upon which to base such a fundamental decision and consistent with the view articulated when debating MOD_09_19 we remain uncomfortable with the lack of reliable evidence.

Consultation Question 3.1) Do you support this Capacity Market option and its implementation in the SEM?

Power NI response:

At a principle level Power NI recognises that it is counterintuitive, inequitable and contrary to the objectives of the capacity mechanism for a generator to be penalised despite being available and ready to generate simply because of a system constraint elsewhere on the network.

Power NI has no comment on the suitability of the approach proposed to resolve this issue.

Consultation Question 3.2) Do you have any concerns regarding the removal of Difference Charges where Operational Constraints are binding, including the risk of unintended consequences? If so, please explain these concerns.

Power NI response:

As a supplier Power NI is concerned by any suggestion that there would be an increase in the 'hole in the hedge' and a further reliance on the Capacity Socialisation Fund. This would need properly assessed and its potential likelihood and impact understood.

The Socialisation Fund is a critical aspect of the market design. Suppliers should not be exposed to the risk the Fund mitigates. Power NI would therefore like to take this opportunity to restate that the financeability and security of suppliers is crucial to the effective operation of the electricity market; all parties including generators and Market Operators only secure their funds via suppliers.

Consultation Question 3.3) Do you consider this proposed change is in keeping with the broader CRM detailed design? Please explain your view.

Power NI response:

Power NI has no comment in relation to this question.

Consultation Question 3.4) Do you have any views on this option from a consumer perspective?

Power NI response:

There is a balance to be struck from the perspective of consumers. An effective capacity mechanism is essential to ensure sufficient generation is available to the market and any unmanageable risk is likely to manifest in cost premiums paid for that capacity. This should naturally be avoided where possible. The SEM Committee therefore should be mindful of this cost balance and seek a fair and equitable outcome which reflects their statutory duties to act in the interests of consumer both in the short and longer term.

Consultation Question 3.5) Do you have a strong view regarding an alternative option which could be implemented, i.e. preferably requiring only a configuration change rather than a system change?

Power NI response:

Power NI has no comment on the suitability of the approach proposed to resolve this issue.

Conclusion

Following the introduction of the amended energy trading arrangements on 01 October 2018 there has been significant instability witnessed in the Central Market Systems, defects in the Balancing Market price and a number of extreme pricing events. This has understandably created high levels of concern within the SEM Committee and participants generally.

Power NI believes it is of paramount importance that the market reaches a stable state as soon as possible. This includes reaching a position in which the actual Balancing Market prices are known and understood. From this position a considered, evidence based review of the Balancing Market Pricing approach should be initiated with a fully engaged market. This review may very well result in previous SEM Committee Decisions being changed however if this followed due process and was based upon robust evidence then this would be justified.

Power NI is concerned by the piecemeal approach which appears to be taking place at present. A number of SEM Committee supported modifications have been progressed via the Trading and Settlement Code Modifications Committee. Power NI does not believe that this partial consultation, partial modification approach is optimal. The Modifications Committee's remit is to enhance the operation and efficiency of the market in line with regulatory policy; it does not and cannot change that policy or previous decisions. Power NI therefore would welcome the SEM Committee adopting the approach described above and initiate a Balancing Market pricing review at a time when sufficient robust evidence is available and through that process give clear policy and

approach direction to the industry. This would avoid making decisions with incomplete inaccurate data and protracted piecemeal discussions taking place at the Modifications Committee. Such a review would be entirely appropriate and consistent with the good governance of a fundamentally changed market.