Trading and Settlement Code Parameters for 2012

Synergen's response to SEM-11-074

1 Introduction

This paper is Synergen's response to the consultation paper "SEM - Trading & Settlement Code - Annual Parameters for 2012 - Consultation" (SEM-11-074). Synergen has no objection to this response being published.

2 Parameters to be Maintained

SEM-11-074 seeks views on five parameters within the T&SC to take effect for 2012. Synergen believes that the existing values should be maintained for:

- MSP Software Penalty Cost Parameters;
- Annual Capacity Exchange Rate;
- The calculation of Uninstructed Imbalances; and
- Flattening Power Factor.

With respect to the Flattening Power Factor, Synergen believes that there is a strong case for reducing this value from 0.35 to a lower value. Synergen's position on this was set out in our response to SEM-11-019, where we set out that any increase in the power factor would increase the lottery effect of the CPM. We concluded that there may be merit in investigating a reduction in the power factor. While the issues raised in SEM-11-019 remain under consideration (including the possible application of separate ex-ante and ex-post power factors, and changes to the power factor value or values) Synergen believes that the existing power factors should be maintained for 2012.

3 Credit Cover

Synergen does not support the proposed changes to the Credit Cover Parameters. SEM-11-074 proposes that the Fixed Credit Requirement for Netting Generators is reduced from the existing level of €5,000 to €1,000 and that the Fixed Credit Requirement for Supplier Units is changed from a fixed €10,000 to a band between €1,000 and €15,000.

The historic analysis set out by the SEMO in SEM-11-074a (2012 SEM Parameters for the Determination of Required Credit Cover) suggests that a €1,000 Fixed Credit Requirement for Netting Generators would cover any historic exposure levels to date, it is not clear to Synergen that given the nature of, and scale of, new generation entry that historic observed exposure levels are necessarily a robust indicator of future exposures. On this basis Synergen suggests that the existing values are retained.

The proposal made in SEM-11-074 is that a scale of Fixed Credit Requirement for Supplier Units ranging between €1,000 and €15,000 should be adopted. The SEMO view is that the proposal to vary of Fixed Credit Requirement for Supplier Units strikes the "best compromise between covering the worst case scenarios and average Market risk at a point in time"[1].

Synergen supports the principle of a range of Fixed Credit requirements. However, its over-riding objective is that the Credit Cover in place should be at the 95th percentile level. The SEMO assessment of Fixed Credit Requirement for Supplier Units notes that, while resettlement may increase or decrease a participant's level of monies owing to the market and that over a period of time this variance may be broadly neutral, "the risk of a supplier exiting the Market with such large resettlement pending is high"[2]. In essence, the SEMO sees supplier default as a significant risk, or even likely. As generators are obliged to sell into the gross pool and thus sell to counterparties not necessarily of their choosing, the markets counterbalancing obligation is to ensure that credit cover arrangements are robust. Synergen believes that there are two possible approaches to achieve this:

1. **The Fixed Credit Requirement for Supplier Units should be increased from €10,000 to €15,000.** This represents the fixed charge level that delivers the 95th percentile level of cover the level beyond which "…higher values would not significantly improve the cover for re-settlement".[3] Synergen considers that Credit Cover is there to provide, if not fully for an absolute worst-case scenario, something high e.g. the 95th percentile principle generally applied, and based on the SEMO data provided, this level of fixed charge would meet that objective.

2. **The sliding scale approach should be adopted, but the €/MWh should be reviewed to deliver Credit Cover at the 95th Percentile level.** In SEM-11-074a the SEMO recommends that a figure of 8.77€/MWh is adopted – this figure reflecting the average of the re-settlement rates over the 16 week period studied by the SEMO. However, it is not clear from the analysis presented what the interaction is between this €/MWh rate, and the Fixed Payment in delivering Credit Cover at the 95th percentile level. Synergen believes that such an assessment should be undertaken.

On balance, Synergen would be comfortable with the variable range of Fixed Credit Requirement for Supplier Units subject to a demonstration that 8.77 €/MWh is consistent with the 95th percentile principle, OR otherwise adopt an alternative €/MWh figure that achieves this level of Credit Cover.

[1] SEM-11-074a page 31
[2] SEM-11-074a page 31
[3] SEM-11-074a page 31