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Commission for Energy Regulation  
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5<sup>th</sup> October 2016

Dear Karen and Thomas,

PrePayPower, as Ireland's largest prepay electricity provider, welcomes the opportunity to contribute to the SEM Committee's consultation on the Capacity Remuneration Mechanism (CRM) Capacity Target and De-Rating Factor Methodology (SEM-16-051).

PrePayPower offers what are effectively fixed prices to our residential customers. This requires managing exposure to changing market prices through hedging in a variety of fashions. The "regulated" elements of this hedging are being covered extensively in the Forwards and Liquidity workstream. These regulated risk management tools to date have included the potential for market maker obligations and forward contract sell obligations.

The CRM also provides a piece to the overall hedging puzzle, namely capping suppliers' exposure to high market prices at the reliability option strike price. Our response wishes to draw out a few key impacts of the proposals in the consultation paper on the "reliability" of the reliability option effective price cap, i.e. draw out potential implications in the failure of the price cap mechanism known as the "hole-in-the-hedge".

So with the exception of the the inclusion of reserve targets in the Capacity Target (and the parallel changed algebra within the I-SEM T&SC) which we support (Question 2.2.1 A – Capacity Requirement), our comments are not directed at the methodology within the papers, but rather the outcomes for suppliers being able to serve customers effectively with the form of tariff that most consumers desire, i.e. risk-managed fixed price tariffs.

While uncertainty continues around the pricing in I-SEM given the removal of the Bidding Code of Practice, an as-yet unproven and untested Balancing Market pricing design, while the allowed forms bidding allowable into the day-ahead market is not yet approved at a European level, and while the Forwards and Liquidity workstream decisions and next steps are delayed and to date has not acknowledged interaction with the CRM implicit price cap, this places greater emphasis on the importance of the CRM to remove volatility from the underlying energy price fundamentals.



We have two objectives from our response:

- The CRM Capacity Target should not put undue downward pressure on generator revenues. This will result in greater energy price volatility as generator focus greater cost recovery into their operating/in merit hours. Reduction in CRM charges faced by consumers will be replaced by increased energy charges which are much more volatile. Even if the reduced quantum of capacity charges were replaced 1:1 with increased energy charges at the wholesale level for a supplier, management of the relative increased risk in the energy price would leave higher net retail costs to the consumer. Downward pressure on the CRM auction target therefore has consequences, and these should be balanced in any CRM decision making. PrePayPower does not have the correct answer in relation to the balance between unduly high CRM payments and potential unmanageable volatility in the energy market. We are merely pointing out that **the interaction of energy market price volatility and capacity revenues, within the context of an uncertain and still emerging I-SEM design (including hedging opportunities) is an important consideration for the SEM Committee's consideration.**
- Interconnectors do not pay CRM difference payments as long as they are technically available. Therefore the greater the obligated capacity quantity on an Interconnector, the greater the "hole in the hedge". While PrePayPower acknowledges State Aid approval requires cross border CRM participation to be addressed, it appears that this State Aid approval has taken primary consideration over cost to the consumer and fair competition between capacity providers.

**PrePayPower urges the SEM Committee to take a highly prudent view on the capability of Interconnectors, i.e. a more aggressive de-rating, so that hole-in-the-hedge issues are minimised.** This is not unduly discriminatory within the context of the special settlement treatment afforded to Interconnectors (no CRM difference payments under normal operation) and the consequences of that interconnector treatment on other market participants (distorting competition, providing poor value to consumers during periods of coincident scarcity, and making the provision of fixed price tariffs to customers more difficult).

Interconnectors are also exposed more regularly (based on historical events) to High Impact Low Probability issues (HILPs), compounding the issue. It is not unreasonable to ask at what point should a "HILP" be considered a "HIMP", i.e. High Impact Moderate Probability and be fully considered within the de-rating of the Interconnectors.

For the avoidance of doubt, our stance on Interconnectors de-rating is purely due to the fact their treatment under current CRM settlement directly impacts PrePayPower's hedging strategy due to the created hole-in-hedge issues. We do not believe that any consumers should face increased risks due to preferential treatment of any technology class, irrespective of what that technology class is.



Finally, we would like to take this opportunity to support the inclusion of reserve requirements in the Capacity Target, and note and welcome the parallel developments in the more recent I-SEM Trading & Settlement Code drafts which includes reserve provision in the Capacity Quantity Scaling Factor. These are the type of prudent and “joined-up” actions which a) ensure the Capacity Target is not unduly depressed and reflects the needs of the system, and b) ensures that generators who are successful in the auction make fair contribution to their cleared capacity quantity and implicitly contribute to “hole in the hedge” issues. We support this level of demonstrated integration across I-SEM Programme workstreams, and hope to see it demonstrated further within the Forwards and Liquidity decision due imminently.

Our response is not confidential and may be published in full. If you wish to have further communication in relation to our submission, please don't hesitate to contact me.

Yours faithfully,

Cathal Fay

