

I-SEM
Capacity Remuneration Mechanism
Parameters for T-4 2022/23 Capacity Auction
Consultation Paper
SEM-18-028

Moyle Interconnector Limited Response

Introduction

Moyle Interconnector Limited welcomes the opportunity to respond to the present consultation on parameters for the T-4 capacity auction for delivery year 2022/23. We find that the paper correctly identifies a series of considerations that would affect the function of the capacity market, but as an interconnector owner we have focussed in particular on arrangements relating to cross-border capacity.

In the table below we have addressed the specific questions in the consultation paper. However, some additional remarks on the treatment of interconnector units are presented here, particularly on the theme of cross-border participation.

Responses to Specific Consultation Questions

2. TREATMENT OF CONSTRAINTS IN T-4 AUCTION	
1) Do you agree with the SEM Committee's proposal to reflect transmission constraints in the T-4 auction? Please explain your rationale.	<p>We agree that it is necessary to include transmission constraints in the T-4 auction. Our reasoning is in line with that of the SEM Committee, particularly:</p> <ul style="list-style-type: none"> • It is clear that without considering locational constraints in the first T-1 auction insufficient capacity would have been procured in Dublin or Northern Ireland. • It is not clear that the North-South transmission constraint will be removed by capacity year 2022/23. • A full suite of reforms to locational signals is unlikely to be in place prior to the auction.
2) Do you have any comment on the possible inclusion of multi-year pay-as-bid Reliability Options to meet the minimum Locational Capacity Constraint requirement?	We offer no view on this matter.
3) Do you have a preference between the options set out above in relation to pay-as-bid offers? Please explain your rationale.	We offer no view on this matter.
3. AUCTION FORMAT	
1) Do you have any comments on the SEM Committee's proposal to move to an auction format based on Auction Format C for the CY2022/23 T-4 auction, following the State aid decision?	While we would be cautious about moving to format C, we recognise the commitment made in order to satisfy the state aid requirements.
2) Do you have any comments on the TSOs proposed AASM for implementing the new auction format, as set out in Appendix A, or the RAs' proposed change to the N parameter?	We offer no view on this matter.
3) Do you have any comment on the proposed change to the format to accommodate multi-year pay-as-bid Reliability Options?	We broadly agree with the proposed approach, noting that lumpiness is an all-island problem, so multi-year offers up to net CONE need not be accepted for lumpiness reasons; and that acceptance of a multi-year offer priced lower than both CONE and competing single-year offers to satisfy a constraint is beneficial.

4. CAPACITY REQUIREMENT

1) What are your views on the potential changes proposed to the CR methodology i.e:

- Incorporate some measure of operating reserves in the CR? What MW value?
- Whether the 8-hours LOLE standard should be tightened (reducing the LOLE target). What level do you consider to be appropriate and why?

We agree that it is appropriate to include operating reserves in the capacity requirement. Although such reserves were not procured in the first T-1 auction due to existence of surplus capacity, it is not clear that surplus capacity will be available by 2022/23, so including operating reserves in the capacity requirement is a natural approach.

Regarding the MW value, we suggest that at least option 2 (250 MW) is required, since this is broadly equivalent to the 3 hours LOLE. In practice, the likelihood that EWIC (the single largest infeed) is importing during a stress event, implies a need to apply option 5 (500 MW).

(Should insufficient reserve be procured to cater for EWIC's full import during a period of stress then the cross-border capacity is likely to be reduced due to the absence of sufficient reserve. Such a situation appears to contradict the European policy direction of maximising interconnector capacity as a contribution to security of supply. Therefore sufficient reserve should be procured to cater for this scenario.)

We agree that the 8-hours LOLE should be tightened, recognising that the operating policies of the system operators on demand control during periods of reduced reserve. In practice, if sufficient reserve is procured, a 3 hours LOLE standard could be achieved.

5. ADMINISTERED SCARCITY PRICING PARAMETERS

1) Which of the options for the value of Full ASP do you consider most appropriate for the first T-4 capacity auction, and why?

We find option A (25% of VoLL) most appropriate for the following reasons:

- Although the equivalent of full ASP in GB is moving to £6000/MWh, that price is a cap, unlike ASP in SEM which is a floor. Therefore there is still significant scope for prices in each market to move between the SEM floor and the GB cap. Moving the SEM full ASP floor to a level approximately equivalent to the GB ASP cap would not allow prices to move freely in an equivalent range during periods of coincident tightness, distorting the effect of the market price on interconnector flows.
- As the consultation paper notes, prices are not the sole determinant of interconnector flows.
- Although the SEM Committee has signalled a move towards VoLL, the integrated market design is not yet live. Therefore until participants have some experience with the market adjustments to such a key parameter should be gradual rather than a significant step change.

2) Should we move to setting VoLL on an October to September year, rather than the current Calendar Year basis, so that a single value of VoLL pertains within a Capacity Year?	It would make sense to calculate VoLL for a capacity year (but its availability for calendar years is unlikely to be major complication for participants).
6. AUCTION VOLUMES AND DEMAND CURVE	
1) Should the proportion of the CR the SEM Committee hold back from the T-4 CY2022/23 auction for the T-1 CY2022/23 be increased from 5% to 7.5%, and why?	We recommend a cautious approach should be taken, in order to avoid potential under-procurement at T-1, since it could reasonably be assumed that many units unsuccessful in the T-4 auction will have closed by the time of the T-1 auction. Therefore the lower end of the range (5%) should be applied.
2) Should the minimum MW in each constrained area be adjusted for volumes withheld from the T-4 auction to the T-1 auction for CY2022/23? Which of Options 1, 2 and 3 do you prefer, and why?	We recommend an efficient but cautious approach. Option 1 (full requirement) is likely to be inefficient through procuring more expensive capacity. Options 2 and 3 each have some merit and we suggest a compromise could be appropriate whereby historic DSU participation would be used, but up to a maximum of e.g. 5%. In this way some capacity is reserved for participation at T-1, but if historic DSU participation in a constrained zone is low then less capacity would be reserved, reducing the risk of under-procurement at T-1.
3) Which of the demand curve options, Options A or B, in your view is the most appropriate for the first T-4 capacity auction, and why?	We express a slight preference for option B (straight line) because for a T-4 auction any shortfall can in theory be made up at T-1.
7. T-4 AUCTION PRICE CAPS FOR CAPACITY YEAR 2022/23	
1) Do you agree with the proposal to keep the Auction Price Cap (APC) at 1.5 x Net CONE for the T-4 auctions? If not, please explain. Is your response in any way contingent upon the final value of BNE Net CONE for CY2022/23?	We offer no view on these matters.
2) Do you agree with the proposal to keep ECPC at 0.5 x Net CONE for the T-4 auctions? If not, please explain. Is your response in any way contingent upon the final value of BNE Net CONE for CY2022/23?	
3) USPC setting: Do you agree with the proposed approach for UFI submissions?	
4) USPC setting: Do you agree with the proposal to apply 2% p.a. inflation projection for estimating costs for CY 2022/23?	

8. DERATING FACTORS	
1) Do you have any views on the proposal of EMDF value of 60% subject to review and update of the analysis for the decision paper?	We recognise the SEM Committee's desire to avoid volatility in the EMDF from year to year and agree that, while a wide range of values result from the RAs' analysis, changes to the EMDF should be incremental rather than substantial in order to send a consistent signal. However, as experience of the market design builds, consideration should be given to increasing the EMDF in line with observed contribution to security of supply from the interconnected market.
2) Do you expect to be applying to qualify a new interconnector between the I-SEM and an external market other than GB?	No, we do not expect to be applying to qualify a new interconnector for this T-4 auction.
3) Do you have any feedback on the issues around transitioning from the interim to the hybrid solution for cross-border trading of capacity?	Yes, please see our comments below this table.
9. NEW CAPACITY INVESTMENT RATE THRESHOLD	
1) Do you agree with keeping NCIRT at €300/kW, in the light of new evidence on BNE gross investment costs? Does your view depend on the choice of BNE reference plant resulting from the Best New Entrant consultation (SEM-18-025)?	We offer no view on this matter.
10. SUMMARY OF PARAMETERS	
1) Do you have any comments on any of the parameter summarised in Table 6, which are not already covered in your responses to other consultation questions?	We have no additional comments on the parameters in table 6.

General Remarks on Treatment of Interconnectors and Cross Border Capacity

Scheduled Outages

We note that scheduled outages of an interconnector unit are planned in close co-operation with the on-shore TSOs, so that they take place away from peak season and are coordinated with scheduled outages of other units. In practice therefore the scheduled outage rate should not be a significant factor in calculating a de-rating factor.

The Hybrid Solution

Our comments on cross-border arrangements for participation in the I-SEM Capacity Market during CY 2022/23 are based on our understanding of the outline in the consultation paper, which is summarised thus:

- At T-4 interconnectors would participate (indeed as today, interconnectors would be obliged to participate) in the capacity auction. Successful interconnectors would be awarded capacity contracts.
- At T-1 cross border capacity would be able to bid into an auction, up to the total capacity awarded at T-4 to the interconnectors.
- By some means the capacity contracts held by interconnectors from the T-4 auction would be transferred to the successful cross border participants in the T-1 auction.

While we note the requirement of the state aid approval to move to explicit cross-border participation, the approach consulted on has some significant implications and outstanding questions remain. For example:

- **What would be the mechanism for transfer of capacity contracts held by interconnectors from the T-4 auction to cross border units that have been successful in a T-1 auction?**

It would seem to be a confusing and bureaucratic exercise to award capacity to interconnectors at T-4 then retrieve those contracts from interconnectors (through a kind of 'compulsory purchase') in order to then (re-)distribute the same quantity through a T-1 auction. (Worse still would be the situation if the interconnector owners were obliged to re-sell, through a kind of secondary trade, their T-4 contracts, including qualification, de-rating, etc. of cross-border units. Those processes are clearly a delivery body role, not for an interconnector owner.) Any such process would appear to require very significant modifications to the Capacity Market Code. It would also complicate accounting matters in the interconnectors, who after T-4 would hold contracts that they would expect to be revoked later.

On the other hand, awarding capacity contracts to interconnectors at T-4 could be a useful approach if there is doubt that suitable cross-border arrangements would be in place by T-1. In such a situation, having had the interconnector units participate at T-4 would be far less disruptive than having no interconnector participation at T-4. If de-rated interconnector capacity had not been procured at T-4, in anticipation of cross-border capacity being procured at T-1, then a much larger procurement at T-1 would be necessary to make up for the under-procurement at T-4. The T-1 quantity to be auctioned would be that which was deliberately reserved for the T-1 auction, plus roughly interconnector size quantities.

- **How would interconnector availability be incentivised?**

If the interconnector units do not hold any form of reliability obligation (through not participating, transferring their obligations to cross-border units, or some other arrangement) there would be a consequent effect on their incentive to be available. This does not appear to be the intent of the I-SEM design. Further, the actions taken by cross-border units to fulfil their reliability obligation will be in practical terms meaningless if the interconnector units themselves are on an outage.

- **How could a cross-border unit demonstrate delivery?**

In the I-SEM design cross-border flows are determined at day ahead by the result of the pan-Europe EUPHEMIA algorithm, which maximises overall economic welfare. The flows can be further altered by the results of the local GB-SEM intra-day auctions, pending

implementation of the XBID solution. In each case it is rational that flows will be determined based on relative prices between the two markets.

The natural question associated with explicit cross-border participation in the I-SEM Capacity Market is how a small number of units holding cross-border I-SEM reliability options can act to change the interconnector flows in order to deliver on an obligation to contribute to security of supply in I-SEM. We observe that since interconnector flows are based on the market price spread and that since the behaviour of a single unit in GB is unlikely significantly to change the market price, the ability of a single unit to be able to demonstrate delivery of power into I-SEM is at best limited. Indeed a single GB unit's response to the I-SEM price (for example by increasing its output) may be 'drowned out' by the response of most other units to a change in the GB price (if a lower GB price causes units to decrease their output).

Conversely, any significant change in interconnector flows due to intra-day price movements cannot be attributed to the behaviour of a single cross-border unit.

- **De-rating of GB units**

At present, participation by interconnector units is based on the anticipated contribution of the interconnected market as a whole, which is reflected in the de-rating factor applied to an interconnector. If explicit participation by cross-border units was to be similarly de-rated, we could expect to see very low de-rating factors, since individual units in a large market are unlikely significantly to influence interconnector flows, for the reasons described above. In short, de-rating for an interconnector providing access to the interconnected market is not equivalent to de-rating of a single unit in the interconnected market. Intuitively one would expect such units to receive very low de-rating factors, which would deter participation. (A further factor potentially influencing participation by GB units is that they have no control over availability of the interconnector.)

- **Interconnectors already deliver cross-border capacity**

In contrast to the challenge of how individual cross-border units can demonstrate delivery (see above), interconnector units themselves already provide access to the security of supply benefits of interconnection to the whole adjacent market. Interconnector flows based on the prices in the interconnected markets are taken into account in the interconnector de-rating, and interconnectors are incentivised to provide access to the external market. This approach has been successfully applied in both GB and I-SEM capacity mechanisms. In the absence of a Europe-wide approach for explicit cross-border participation, participation in the capacity market by interconnector units remains an efficient option which is compatible with implicit scheduling of interconnector flows.

- **Cross-border cooperation**

We note that opening the I-SEM capacity market to cross-border capacity depends on quite significant engagement and cooperation with the neighbouring regulatory authority and capacity market delivery body and might also require non-trivial changes to the capacity market design in GB, such as changes to rules and underlying regulations. At a time when the regulatory agenda is quite busy, we suggest the challenges of such cooperation should not be underestimated.

Conclusion

Arrangements for cross-border participation require further thought in order to develop a practical, efficient and appropriately incentivised approach. The contribution to security supply provided through interconnector units should continue to be recognised in the CRM. We stand by to assist the RAs with such a project. Meanwhile we recommend full interconnector participation at T-4 auctions to avoid distortions of the market if practical and efficient arrangements for explicit participation by cross-border units cannot be adequately developed by T-1.