



Energy for
generations

Generation & Wholesale Markets

ESB GT Response:

**Capacity Remuneration Mechanism (CRM) Reserves
Consultation Paper (SEM-18-159)**

2nd November 2018



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1. INTRODUCTION

ESB GWM welcomes the opportunity to respond to the CRM Reserves Consultation Paper (SEM-18-028). In the T-4 parameters decision paper (SEM-18-155), the SEM Committee decided to procure capacity to cover a measure of reserves in the CY 2022/23 T-4 auction. The SEM Committee decided that the measure should be no less than 100 MW and no more than 500 MW at the all-island level. The purpose of the Consultation Paper is to consult on whether reserves should be included in the Local Capacity Constraint Area (LCCA) and if so what approach should be used to determine the MW value for the (a) 2022/23 T-4 auction and (b) the 2019/20 T-1 auction. Any decisions from this consultation are expected to be implemented in the CY 2019/20 T-1 final auction information pack due at the end of November.

ESB GWM's response is broken into two sections; the first is an executive summary of ESB GWM's response to the Consultation Paper and the second section lists ESB GWM's response to the questions in the Consultation Paper.

2. EXECUTIVE SUMMARY

ESB GT believes the SEM Committee's decision to include locational constraints in the CRM T-4 auction is not the most suitable approach for addressing the locational transmission constraints in I-SEM. As far as ESB GT is aware, there are no other capacity markets that (a) apply locational constraints in a non-zonal auction or (b) create the perverse outcome of unsuccessful in-merit winners.

ESB GT does not believe the potential implications of including locational constraints in the CRM auctions have been considered sufficiently to support the decision. ESB GT requests the SEM Committee to review if the decision to allow locational constraints in the T-4 auction acts to undermine the ISEM high level design. For example, it is reasonable to assume where new entry is contracted for locational requirements it won't result in a high clearing price for the unconstrained market. This outcome effectively splits the market between new and existing generators which could reduce competition and lead to an inefficient price signal. The lack of a high clearing price, in auctions with new capacity, will result in their being no light on the horizon for the marginal incumbent generator and so no way for the incumbent marginal generator to recover sunk costs, resulting in this unit getting an early exit signal at the same time as the TSO are contracting for locational new entry. The potential return for incumbent generators is now limited because of interventions. The market design impact means the new entry locational capacity being built to run is peaking or recip capacity and the SEM Committee's decisions are pushing mid merit plant off the system in favour of peaking products/DSUs in locational constraints areas which in the longer term will drive up energy prices.

ESB GT believes it would have been beneficial to perform a review¹ of locational signals, as per ESB GT's response to SEM-18-028 and the SEM Committee's CRM T-4 Parameters decision (SEM-18-155), which could have created an enduring solution that could have been implemented for the T-2, T-3 and T-4 auctions. The logic that "*if the auction was delayed beyond the 3 and ½ year lead time will increasingly preclude new entry from certain technologies that take a time to build*"² does not align with the SEM Committee decision to "*maintain the status quo of allowing the possibility of multi-year pay-as-bid Reliability Options only where there are no other solutions available to satisfy the minimum MWs in the constrained area*"³, which does not encourage new investment in local capacity constrained areas.

ESB GWM requests the SEM Committee to review the decision on the "compensation for unsuccessful winners" if the SEM Committee decide to implement locational transmission constraints in the T-4 auction.

¹ CRM Parameters for T-4 2022/23 Capacity Auction Decision Paper (SEM-18-155) point 2.4.3 "The SEM Committee agree with those respondents who suggested that a full review of locational signals is appropriate..."

² SEM-18-155 point 2.4.4

³ SEM-18-155

The inclusion of locational transmission constraints is resulting in a perverse auction outcome where an in-merit winner is unsuccessful in obtaining a capacity contract and receives no compensation without any acceptable justification.

Considering the timeframe between the results from the first CY 2018/19 T-1 auction and the publication of this consultation, ESB GT believes an enduring solution for all of the possible approaches for determining the measure of reserves in LCCAs should have been consulted upon, not a bottom up approach based on “rule of thumb”. The lack of a methodology for the bottom up approach leaves participants in a difficult position of passing comment and selecting a preference from three options when the methodologies are still opaque i.e. point 3.2.4 “*the SEM Committee may choose to include a measure of reserves in the CY 2019/20 demand curve at all-island level, but if it does, this measure is likely to be lower than the amounts employed for the CY 2022/23 T-4 auction*”.

ESB GT believes the constant changing of CRM rules and subsequent modifications to CMC is creating significant regulatory uncertainty. The uncertainty from rules changing from auction to auction does not provide stability required for investors with a long term project nor does it provide sufficient signals to promote competition.

Finally, ESB reserve the right to revise our comments on this consultation response if the forthcoming “bottom up” approach does not meet the assessment criteria for the CRM; competition, equity, stability, efficiency and practicality/cost⁴.

3. RESPONSE TO CONSULTATION QUESTIONS

In this section ESB GT has listed its response to the questions from the Consultation Paper.

3.1 Inclusion of Reserves in CY 2022/23 T-4 Auction

Q. 1) Do you agree with the proposal to include reserves in Locational Capacity Constraint Area minimum MWs for the T-4 CY2022/23 capacity auction? Please explain.

As per ESB GT’s response to the T-4 Parameters Auction consultation (SEM-18-028), ESB GT agrees with the inclusion of reserves in the T-4 capacity requirements considering the change in the auction format⁵. However, ESB GT believes the SEM Committee’s decision to include locational constraints in the CRM T-4 auction should be used for addressing the locational transmission constraints in I-SEM. As far as ESB GT is aware, there are no other capacity markets that (a) apply locational constraints in a non-zonal auction or (b) create the perverse outcome of unsuccessful in-merit winners. Rather than the proposed auction format C⁶ ESB GT believes it would have been more beneficial to postpone the T-4 Auction in order to perform a review⁷ of locational signals, as per ESB GT’s response to SEM-18-028 and the SEM Committee’s CRM T-4 Parameters decision (SEM-18-155), which could have created an enduring solution that could have been implemented for the T-2, T-3 and T-4 auctions. ESB GT is still of the view that there are more suitable market based solutions for addressing the locational transmission constraints and that there is still time to develop a solution before the T-4 auction while remaining State Aid compliant.

Considering there is still time before the CY 2022/23 T-4 auction, ESB GT believes the SEM Committee’s proposal to hold a consultation on methods to solve the locational issues would have been better to have

⁴ SEM-18-159 Section 1.3

⁵ SEM-18-159 point 3.5.1

⁶ SEM-18-159 point 3.5.1

⁷ CRM Parameters for T-4 2022/23 Capacity Auction Decision Paper (SEM-18-155) point 2.4.3 “The SEM Committee agree with those respondents who suggested that a full review of locational signals is appropriate...”

brought forward than this current consultation on a CRM structure that ESB GT does not believe should be part of the CRM design considering the significant subsequent consequences⁸.

Q. 2) If reserves are to be included across the Locational Capacity Constraint Areas, which of the above approaches (or other approaches do you favour and why)?

If the SEM Committee intends to implement the locational constraints zones in the CY 2022/23 T-4 auction, ESB GT agrees that the bottom up approach provides greater flexibility than the top down approaches, a valuable functionality for the Regulators, whereas the top down approaches provides greater transparency and simplicity, both of which are important to market participants. ESB GT believes a bottom up approach is the most suitable methodology available for achieving the assessment criteria for the detailed design of the CRM as set out in section 1.3 of the consultation paper once it is implemented with full transparency. The current proposal that “*it may be necessary to implement a bottom-up type approach using some “rule of Thumb”*” is not appropriate as it generates greater uncertainty and a lack of replicability. ESB GT requests a detailed methodology to be consulted upon and published if the bottom up approach is to be implemented.

3.2 Inclusion of Reserves in CY 2018/20 T-1 Auction

Q. 3) Do you agree with the proposal to include reserves in the forthcoming T-1 capacity auction for CY2019/20? Please explain.

Please see response to Q1. ESB acknowledge the timelines for the T-1 auction CY 2019/20 are tighter than those of the T-4 auction CY 2022/23 for performing a review⁹ of locational signals. ESB GT request full transparency of any methodology that could be used for including reserves in the forthcoming T-1 capacity auction.

In response to T-1 specific factors that were listed in the consultation, ESB GT believes a fully functioning secondary trading market could help alleviate some of these concerns. ESB acknowledge that a secondary traded market is listed as a day 2 action to be addressed but ESB GT would like to take this opportunity to highlight the importance to have this implemented as soon as possible.

Q. 4) Do you agree with the view that the case for including significant reserves in the all-island demand curve is relatively weak?

See response to Q3.

Q. 5) If reserves are to be included across the Locational Capacity Constraint Areas, which of the above approaches (or other approaches do you favour and why)?

Please see response to Q2. ESB GT acknowledge the timelines for changes to parameters of the T-1 auction CY 2019/20 are tighter than those of the T-4 auction CY 2022/23. However, for the remaining interim

⁸ LRSA

⁹ CRM Parameters for T-4 2022/23 Capacity Auction Decision Paper (SEM-18-155) point 2.4.3 “The SEM Committee agree with those respondents who suggested that a full review of locational signals is appropriate...”

auctions (CY 2020/21 and CY 2021/22) if LCCA are applied to each of the auctions ESB GT would expect to see a more transparent MW approach applied until a new methodology for dealing with the locational constraints is developed.

Q. 6) Are there reasons to use different approaches for the CY2019/20 T-1 auction and the CY2022/23 T-4 auction? If yes, please explain.

ESB GT believes for regulatory certainty and continuity required for the CRM a single approach, which is fully transparent and repeatable by all market participants, should be applied to both the T-1 and T-4 auctions.