ESB GT Response:

Dublin Security of Supply: Locational Scarcity Scalars for System Services in the Dublin Region

19th March 2017

General Comments

ESB Generation and Trading (GT) welcomes the opportunity to respond to the CRU consultation on the application of locational scalars for the provision of system services in the Dublin region.

Throughout the development of the ISEM design CRU, in GWM's view, focused on the development of a competitive framework for the procurement of capacity to meet the system security standard set by the TSO based on the energy market merit order and related unrecovered fixed costs. Implicit in this view of the market is that the system acts as a copper plate with each MWh and MW being homogeneous. Where transmission constraints exist they were viewed solely in terms of local market power with a series of market interventions developed to mitigate the potential for the abuse of this perceived market power. The ambition for the cumulative effect of these measures has been to bring existing generators that are outside of definition of in-merit capacity but behind a transmission constraint to be held at point of indifference until the transmission constraint can be relieved for any plants that are not in receipt of a TCM or LRSA.

The operation of a large generation plant results in significant commercial and regulatory risks which any economically rational investor would require at least the potential of earning an appropriate reward in order to undertake. Where a generator has effectively been appropriated to act a support the network and maintain the system within standard but left carrying these commercial and regulatory risks the natural result will be for the generator to exit the market.

Where this exit results in new entry being required to resolve the transmission constraint given the timescale to implement transmission re-enforcement then the exit signal given by the current market arrangements is inefficient. In recognising that given the constrained nature of the transmission system and the forecast demand growth there is a value to the system of ensuring there is an incentive for existing and new system service providers to locate in the Dublin region ESB GT welcomes what is believed to be an acceptance by the CRU that there is a need to re-balance the distribution of the value created in resolving transmission constraints between end users and the relevant generators so as to ensure the signals seen by existing and new generation capacity both to maintain the resilience of the system and support the transition to a low carbon economy.

The application of locational scalars for system services in a constraint area is a potentially effective mechanism to achieve this rebalancing and ESB GT welcomes its adoption by the CRU. However ESB GT is concerned that the consultation paper does not detail the analysis applied in determining the value of €12.5mill per annum. ESB GT asks that this analysis and the underlying assumptions be shared with industry.

The application of locational scalars for system services in the Dublin Region was one of a suite of mitigation measures the CRU have decided to progress resulting from the DMILC risk of the Huntstown units as set out under CRU/18/228.

Under CRU/18/228 the structure of the LRSA contract to be entered into by Eirgrid with each of the Huntstown units was set out as the total revenue received under the LRSA equals the contract strike price minus any RO revenue and less any revenue from location payments where they were to be introduced. ESB GT would ask that the CRU confirm if the revenues resulting from the application of locational scalars will be netted off the value of the LRSA contracts for those units contracted under this mechanism. On the

basis that this is the case there is potential for the process to become an accounting exercise where the locational scalars substantially only acting to reduce the book cost of the LRSA contracts.

Additionally under CRU/18/228 the potential of Eirgrid to contract with an existing market participant to relocate generation capacity to the Dublin region was discussed. The paper set out that this contract was progressing towards conclusion and that further information would be published in the coming weeks, ESB GT requests that the position in relation to this contract be clarified and where it is or how it is to be progressed along with the structure of the contract, and the mechanism whereby it avoids market distortion, be published.

As recognised in the consultation paper there is a close interaction between the application of locational scarcity scalars for system services and the CRM, and the related USPC process. It would be counterintuitive if, in the case of units that undergo the USPC process in the Dublin regional, the value resulting from the application of locational scalars were to act only to reduce the level of USPC applied to these units. When this were allowed to arise it would result in a transfer of value from the D-TUoS customer in Ireland to the overall SEM capacity market by using the increased D-TUoS charges to potentially reduce the clearing price in the capacity market and arguably this would be a distortion of the capacity market price. As such it is ESB GT's view that in order to avoid this distortion the value of locational scarcity scalars should not be included in the USPC process.

Consultation Questions

Question 1: Do you have any views on the CRU's objectives and principles in relation to introducing locational signals to Dublin via the System Services Locational Scarcity Scalars?

As detailed above ESB GT understands CRU objectives in the introduction of locational scarcity scalar and supports the proposed principles. In ESB GT's view where a service provider is delivering a significant value to the system through their service provision the overall market arrangements should allow for the service provider to be appropriately and separately rewarded.

Question 2: Do you have any comments on the CRU's determination of the amount to allocate to cover the costs of adjusting the System Services Locational Scarcity Scalars in the Dublin Region?

ESB GT asks that the CRU publish the analysis and assumption that underlie the determination of €12.5mill per annum as an appropriate amount. ESB GT welcomes CRU recognition that there is significant value created by generation which provides system services through the postponement of transmission re-enforcement or through the avoidance of interruption to supply of end users in Dublin. In aggregate the market arrangements must allow for this value to be shared between end users and generators to ensure the efficiency of the resulting market signals.

Clarity is sought on the process and assumptions the TSO will apply in determining the scalar value and whether it is intended for a single scalar value to be applied across all of the services or if a different scalar value will be determined for each service?

Question 3: Do you have any comments on the CRU's proposals to adjust the Locational Scarcity Scalars for the above services? Are there other considerations the CRU should take into account in determining the appropriate services?

ESB GT considers that there is a value to system stability in having the inertia on the system distributed across the system to the greatest extent possible to mitigate against inter-area oscillations as such it is proposed that SIR be added to subset of services which the locational scarcity scalar would be applied.

Question 4: Do you have any views on the CRU's proposal to set the Locational Scarcity Scalar values for a five-year period on an ongoing annual basis?

ESB GT supports the CRU's objective to give assurance to the market that once established the locational scarcity scalar while subject to annual review will be set five years in advance. It is considered that in order for investors to factor the impact of the locational scarcity scalar into their plans a strong degree of investor certainty is required.

ESB GT is concerned that the proposal that any over or under-expenditure incurred in one year may be accounted for in the scalar values for the subsequent year and that EirGrid would have the right to adjust the Locational Scarcity Scalar values if there is significant over-expenditure in a particular tariff year act against this objective. Instead investors are placed at risk where the TSO under forecasts or makes an error in setting the scalar value. ESB GT proposes that any under or over recover be factor into the scalar being determine to apply in five years' time.

Question 5: Do you agree with the CRU's proposals in relation to the payment basis for the System Services Locational Scarcity Scalars?

ESB GT does not support the application of the same payment basis as the temporal scarcity scalar. Under SEM-18-032 the temporal scarcity scalar will only be applied to payments related to the market position for providers registered in the energy market. Applying this decision to the locational scarcity scalar in the Dublin region will limit its application to mid-merit service providers and off-line service provision. This would act against the stated of objective to increase remuneration for the services that most contribute to support security of supply in Dublin, where a generator is being constrained on to provide services it is counterintuitive that the services provided would be deemed to be of less value to the system.

Question 6: Do you have any views on how additional revenues received by providers from the application of the Locational Scarcity Scalars should be considered in relation to the CRM and the calculations of a unit's Unit Specific Price Cap (USPC)?

The propose of the USPC process to act a local market power mitigation measure. Where the impact of the locational scalar is factored in the USPC process the impact of the scalar will become a transfer of

value from the D-TUoS customer in Ireland to the overall SEM capacity market by using the increased D-TUoS charges to potentially reduce the clearing price in the capacity market.

ESB GT has a number concerns in relation to the current USPC process and its impact on the market. Specifically in relation to the evaluation of service provision with the USPC process ESB GT believes that the process acts to disincentivise investment by generators subject to the process in increasing their service capability. To correct this is proposed that service provision evaluation should be based on the level of Grid Code connection service capability requirement. Additionally, ESB GT believes that both the temporal and locational scarcity scalars should apply to constrained on service provision and that the impact of these scalars should not be included in the USPC process. In this way generators will retain an incentive to invest in services provision (separately to security provision) in excess of the Grid Code requirement and maintaining this expanded service availability.

Question 7: Do you have any further comments or are there any other considerations the CRU should take into account in its proposals?

No additional comments

Should you have any queries please do not hesitate to contact me.

Yours sincerely,

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William Carr

Regulation, ESB Generation and Trading