



**Electric Ireland Response to  
DCCAIE Proposed Decision Paper:**

**Electricity Support Schemes: Transitioning to  
I-SEM Arrangements**

11<sup>th</sup> Jan 2018

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## 1. RESPONDENT'S DETAILS

Electric Ireland's contacts for any clarifications or questions are given in the table below.

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## 2. GENERAL COMMENTS

Electric Ireland welcomes the opportunity to respond to this proposed decision paper on renewable support arrangements in I-SEM.

Electric Ireland are keen that the final solution achieves a pragmatic and workable arrangement which supports the successful operation of I-SEM while balancing the commercial outcomes for both existing supported wind generators and the final consumer who underwrites the PSO Levy. In particular Electric Ireland agrees that, *where contractually feasible*, supported wind generators representing a significant proportion of all generation should not be immunised from balance responsibility and other obligations inherent in the new I-SEM markets.

Electric Ireland supports the proposed decision to implement option B (blended price) on the basis that it provides a strong incentive for DAM participation but also reflects the reality of imperfect wind forecasting at the day ahead stage. It also strikes, we believe a fair balance between wind generators and the final consumer in commercial terms.

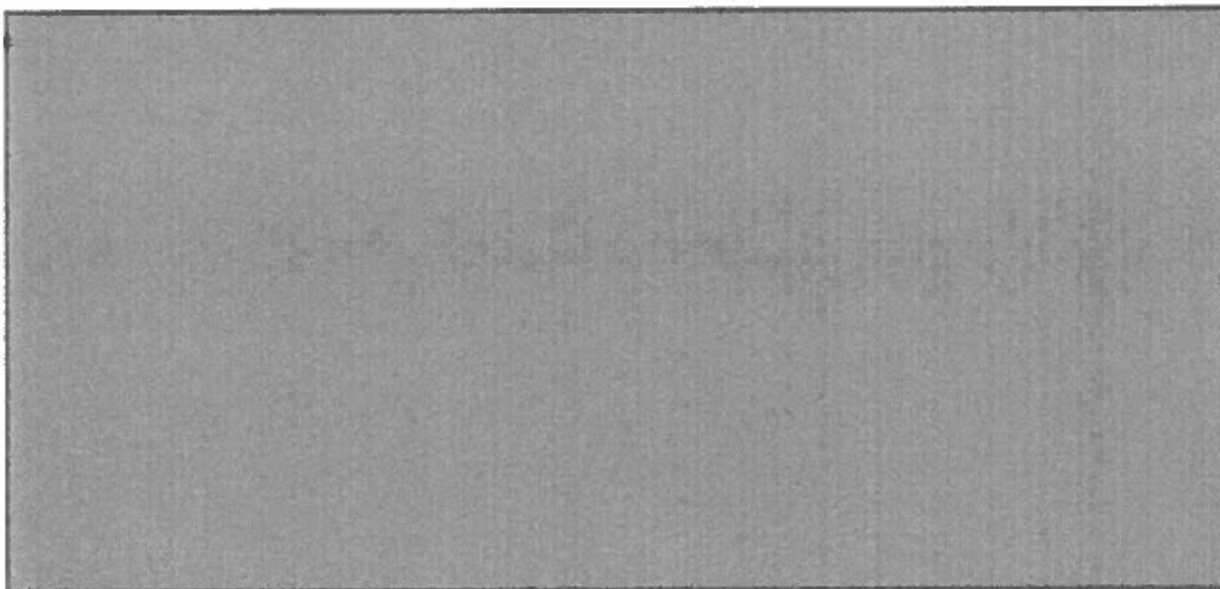
Electric Ireland is strongly of the opinion that a different solution is required for generators receiving Public Service Obligation (PSO) support under the Alternative Energy Requirement (AER) scheme to that proposed for REFIT generators and proposes an alternative solution below. Electric Ireland believes that there are important contractual differences between the AER and REFIT arrangements that make a different solution for AERs necessary. In particular, unlike for REFIT generators, there are no contractual mechanisms available to enable I-SEM imbalance costs, initially accruing to AER suppliers, to be recovered from AER generators. Further, the PSO in respect of AER was imposed directly on ESB by statute (i.e. it did not elect to participate in these contracts). It is a requirement of the PSO legislation (and consistent with the state aid notification) that ESB should be entitled to recover the additional costs



associated with participating in these contracts. We consider that the absence of any mechanism for ESB to recover the balancing costs is contrary to this requirement.

### 3. RESPONSE TO PROPOSED DECISIONS

#### 3.1 Proposed Decision 1 – Blended Approach



Electric Ireland's preference is for the Blended Approach (Option B) as described for the following reasons:

- efficient system operation – wind generators continue to have a strong incentive to participate in the DAM (and this is arguably more realistic objective than Option A's 100% DAM) which supports efficient operation and reduces the additional costs of reversal of interconnector imports as wind participates in later timeframes; wind curtailment is minimised (equivalent to Option A) as shown by EirGrid's analysis<sup>1</sup>; option B also supports a robust DAM reference price (for CfDs etc) due to high DAM liquidity;
- consumer value for money / investment stability – Option B represents a compromise in terms of consumer PSO Levy costs: given EirGrid's modelling assumptions, consumers likely pay more than under Option A (less than Option C)<sup>2</sup> while wind generators are faced with a balance responsibility incentive but without substantially eroding their revenue expectations (and so supporting investment confidence) – in the long term maintaining a balance responsibility incentive for such a large

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<sup>1</sup> Comparison of Proposed REFIT Schemes in I-SEM, Figure 4, p24

<sup>2</sup> Comparison of Proposed REFIT Schemes in I-SEM, Figure 8, p27

proportion of the generation fleet will provide downward pressure on overall system costs to consumers;

- the 70 / 30 blend for generators below 5MW reflects the additional practical difficulties in procuring real time data for these generators to support wind output forecasting and accurate adjustments to their contracted suppliers' DAM / IDM bids.

Overall Electric Ireland believes that the Blended Approach supports efficient system operation which will deliver efficient overall consumer energy costs while retaining strong participation and balance responsibility incentives for wind generators without prejudicing investment confidence.

### 3.2 Proposed Decision 2 – Other Generation

**Proposed Decision 2:**

The market revenue calculation for the purposes of calculating the PSO levy for other supported generation (under REFIT 1, REFIT 2, REFIT 3 and the Peat PSO Scheme) will be amended to adapt to the Integrated Single Electricity Market.

For these generators (peat, hydro and biomass) supported under the PSO levy, the market revenue calculation for the energy component will be based on the Day Ahead Market Price.

Electric Ireland believe that a blended approach would also be appropriate for non-wind generation that are, of necessity, exposed to imbalance costs in the I-SEM. The blend ratio may be different depending on the technology.

### 3.3 Proposed Decision 3 – Capacity Market Costs

**Proposed Decision 3:**

For all supported generation, capacity market costs will not be included in the calculation of market revenues for PSO levy calculation purposes.

Electric Ireland agrees that any capacity revenues but not capacity costs (e.g. difference charges) should be included in the calculation of market revenues relating to REFIT-supported wind generation for PSO Levy calculation purposes.

State Aid rules require that any capacity income should be included in the calculations. Including capacity market costs (e.g. difference charges) in the calculations would insulate REFIT-supported generation and undermine capacity market incentives which would be unacceptable.

However, the reality as acknowledged in the paper, is that no REFIT-supported wind generation will have the incentive to participate in the capacity market while they are not mandated to participate: there is no more upside than not participating (topped up to the same reference price) but where there are potentially significant downsides: having to make difference payments when there's no wind. This is evidenced by less than 20MW of de-rated wind generation capacity (equivalent to ~195MW of installed capacity) *qualifying* for the first capacity auction.

Unfortunately, the ultimate consequence of this forced decision, is that consumers will continue to remunerate supported wind generators at SEM capacity price levels (rather than at competitive I-SEM levels) for the duration of their renewable support contracts via the PSO.

#### **4. APPLICATION OF PROPOSED REFIT SOLUTIONS TO AER GENERATION**

Electric Ireland (EI) is strongly of the opinion that a different solution is required for generators receiving Public Service Obligation (PSO) support under the Alternative Energy Requirement (AER) scheme to that proposed for REFIT generators. EI proposes an alternative solution below.

Power Purchase Agreements (PPAs) were imposed upon Electric Ireland, and other suppliers, in respect of AER generators by way of a Public Service Obligation. Currently, any additional costs (or surpluses) arising from purchasing power produced by AER generators at the contracted prices are recovered from (or passed back to) the PSO Levy so that the contracting supplier, *in fulfilling the PSO*, is held neutral with respect to market costs.

In its Proposed Decision Paper, the Department states in section 3.6 that:

*“similar amendments will be required to the regulatory documentation for other supported generation under the PSO levy, in particular those supported through the AER and REFIT 3 schemes”*

... but then does not set out what these amendments might be.

EI believes that there are important contractual differences between the AER and REFIT arrangements that make a different solution for AERs necessary:

- AER arrangements mean that revenue surpluses as well as shortfalls are passed back to the consumer via the PSO Levy;
- AER contracts, unlike REFIT contracts, do not anticipate any balancing activities and there is no concept of a 'balancing payment' attributable to the supplier within the PPAs; and
- there is also no market change clause in the AER contracts that would assist with the implementation of I-SEM.

Consequently, unlike for REFIT generators, there are no contractual mechanisms available to enable I-SEM imbalance costs to be shared with AER generators. In addition, even if there was, there would be significant practical difficulties involved in contacting and negotiating with particularly the de minimis AER generators at this stage in the lifecycle of their contracts.

The proposed arrangements for REFIT generators, if applied to AER generators, would mean that all of the imbalance costs arising from intermittent AER wind generation would have to be borne by EI as the contracting supplier. This applies directly in the case of in-market AER generation (e.g. Arklow Banks) but also indirectly in the case of de minimis AER generation where imbalance costs occur if the expected de minimis generation is not deducted from the demand forecast used to inform supplier ex-ante market trading.

EI maintains that extending the proposed REFIT decision to also cover AER generation represents a departure from the current situation where the contracting supplier fulfilling its PSO is held neutral to market costs. It is inappropriate to impose such an irrecoverable cost on suppliers who were required to enter into such contracts primarily to provide a route to market for the generators.

Section 39 of the Electricity Regulation Act 1999 as amended, provides for the recovery, by way of a levy on final customers, of the additional costs "associated with complying with a PSO order". The PSO in respect of the AER contracts is imposed on ESB pursuant to the terms of the Public Service Order 2002, as amended. It is a key principle of the 1999 Act and the PSO Order that ESB is entitled to recover the "additional costs" associated with complying with the public service obligation in respect of the AERs. ESB assumed its obligations under the AER contracts on this basis and understanding.

It is not compatible with the requirements of the legislation (nor indeed consistent with the associated state aid notification) that ESB should be precluded from recovering a significant cost (i.e. the balancing cost) which arises solely by virtue of its assumption of the PSO in respect of the AER contracts. This is an additional cost arising by virtue of the public service



obligation. Accordingly, we respectfully submit that the current proposal to disallow this cost for the AER contracts would be contrary to the statutory requirement that ESB must be compensated for its additional costs associated with these contracts. As noted above, we consider that this is to be distinguished from the position for REFIT contracts where there is a built-in mechanism for recovery of a balancing cost in the contract.

Electric Ireland's proposal as set out in this submission is entirely compatible with the State Aid notifications underpinning the AER contracts

#### **4.1 Alternative AER Proposal**

El sets out below an alternative proposal to apply to AER generation.

This proposal allows the contracting supplier to recover imbalance costs via the PSO levy and maintains the current principle into I-SEM that the contracting supplier should neither gain nor lose from fulfilling its PSO to purchase the output from AER generation.

Essentially the difference between the (energy and capacity) price paid to the AER generator and the (energy and capacity) price received / avoided from the market will be reclaimed from or paid back to the PSO Levy.