Response by Energia to SEM-23-080

Supplementary Consultation Paper on modified and combined Modifications to Facilitate Delivery of Capacity

20 October 2023

Executive Summary

Energia is opposed to the modification proposals in consultation paper SEM-23-080. The proposals are unfair and uncompetitive as they retrospectively change key terms of concluded auction processes. The proposals are contrary to the recommendations in ACER's October 2023 report[1] that national authorities should ensure penalties are applied to properly incentivise new capacity providers to commission contracted capacity in a timely manner. Finally, the proposals reduce transparency in the operation of the SEM and are contrary to the objective to ensure no discrimination between participants. For these reasons, the modification proposals should be rejected, or at the very least brought to a CMC Workshop with legal drafting for full scrutiny and consultation.

Energia has consistently opposed modifications that are retrospective in effect and fundamentally change the key terms of concluded auction processes. Energia has argued that these modifications are unfair and uncompetitive as the outcome of the auctions may have been different had the changes been in place at the time of the auctions. To substantially change delivery risk in order to favour auction winners is contrary to the CMC objectives to promote competition and to ensure no undue discrimination between participants.

In October 2023, the EU's Agency for the Cooperation of Energy Regulators (ACER) released a report on the security of EU electricity supply. In that report, Ireland was specifically highlighted for not providing appropriate incentives to guarantee delivery of contracted new capacity. The failure to commission new capacity on time "led to the deterioration of the security of supply outlook….and the implementation of emergency actions that came with a significant cost tag for consumers". On the subject of delivering new capacity, the report goes on to note the importance of "well designed, non-delivery penalties" and that the failure to implement these could "lead to less robust offers by market participants". SEMC's proposals to ensure the delivery of contracts from certain auctions are contrary to the recommendations from ACER.

The modification proposals fail to provide for transparency in the SEM. There is no discussion in the proposals of what details SEMC would make public regarding its decisions on whether to approve extension requests or not. Without such information, it will be more difficult to ensure that SEMC's decisions on whether or not to allow participants extensions are consistent, ensure no undue discrimination, and what the general expectations are regarding under what circumstances SEMC will consider delays to be permissible or not.

The modifications proposed by SEMC are materially different from any modifications that have been discussed at a previous CMC Workshop. Nor has SEMC provided legal drafting for the proposals. Furthermore, it is unprecedented that the RAs would seek to consult upon a modification that may directly impact on the fundamental terms of a current CRM auction while that auction is ongoing, and this could have a potentially distortive impact on the bidding process.

Given that there are significant concerns regarding these proposals' compatibility with the objectives of the CMC, SEMC should not approve these modifications and instead

[1] Security of EU electricity supply 2023 (europa.eu)

should bring any revised modification through a CMC Workshop with legal drafting noting that all previous modifications to the CMC have been progressed in this manner.

1 Introduction

Energia welcomes the opportunity to respond to SEM-23-080 on modifications to facilitate delivery of new capacity.

Energia has actively contributed to CMC Workshops, and responded to consultations, on outstanding modifications that seek to allow for extensions to the delivery of awarded capacity. Energia recognises that the CMC allows the RAs to make a modification that is materially different from a proposed modification. However, the lack of legal drafting provided, the absence of a specific workshop, and the short timeframe permitted for consultation responses, does not allow for the level of discussion and scrutiny required on whether modifications of such significance facilitate the objectives of the CMC.

This is in addition to our concerns that the proposed modifications may significantly change the delivery risks of the current T-4 27/28 auction, and thus the bidding behaviour of participants. It is unprecedented that SEMC would consult upon fundamental changes to the terms of an auction while that auction is underway. In previously providing clarifications on auctions rules, the SOs have re-iterated the importance of not unduly causing confusion among participants on the rules of the auction. For the RAs to progress this proposed modification mid-auction would seem entirely contrary to this intention and is likely to encourage adverse selection in favour of less-prudent bids.

This response will firstly set out Energia's objections to the proposed modification on the grounds of its retrospective effect in changing fundamental terms of concluded auction processes. This response will then set out why the proposed modifications move Ireland further away from best practice as described by the EU Agency for the Co-operation of Energy Regulators (ACER), and in doing so fail to facilitate the development of the CRM in the short and long-term interests of consumers. Finally, this response will discuss why the modifications as set out do not facilitate the CMC objectives of providing transparency, ensuring no undue discrimination between parties, or promoting competition.

2 Retrospective Effect of Proposed Modifications

Section B.12.15 of the CMC requires that modifications to the CMC shall not have retrospective effect. Energia has consistently argued that all modifications that seek to retrospectively alter the fundamental terms of concluded auction processes are retrospective in effect.

At the time of the relevant auctions that are being considered for this modification participants that were considering bidding for New Capacity contracts understood that projects that failed to meet their delivery milestones were at risk of effectively reducing the length of their contract or of termination. Specifically, contracts would end ten years after the start of the relevant capacity year, and would be terminated if Minimum Completion had not been completed by the Long Stop Date, eighteen months after the start of the relevant Capacity Year.[2] The binding delivery conditions and milestones were important in discouraging speculative bids from displacing achievable offers in

[2] Following modifications approved by the RAs in January and June, certain changes were made prior to the T-4 2026/27 and T-4 2027/28 capacity auctions, but the changes in the proposed modification go further still.

the CRM, and in recognising the costs to consumers of failing to deliver capacity on time.

The proposed modifications in SEM-23-080 fundamentally change the delivery risk for the winners of the concluded auctions. Had these changes been in place prior to the auctions, it may have changed the calculation of those considering whether to bid and ultimately the outcome of the auctions. To change the conditions of concluded auctions is retrospective in effect to the benefit of auction winners and is clearly unfair on other auction participants and contrary to the objectives of the CMC to ensure no undue discrimination. On this basis, Energia firmly opposes the modifications proposed in SEM-23-080.

3 ACER Review of Capacity Mechanisms

In October 2023 the Association for the Co-operation of Energy Regulators published, as required by the EU Clean Energy Package, a report on the security of EU electricity supply. The report was a comprehensive EU-wide study and included a review of existing EU capacity mechanisms.

Section 5.3.2.1 of the report focused on non-delivery penalties in the Irish capacity mechanism. The report noted the following:

"This case study provides strong evidence about the benefits of well-designed, non-delivery penalties to ensure developers have the right incentives in place to ensure their capacities are delivered on time. On the other hand, lenient penalties could lead to less robust offers by market participants. Ultimately, if new resources fail to be commissioned on time, this could have severe repercussions for security of supply and lead to significantly higher costs for consumers".

The report's recommendation is that national authorities should ensure that penalties in capacity mechanisms properly incentivise capacity providers to commission the contracted capacity "in a timely manner".

As stated in SEM-23-080 itself, delivering on the T-3 2024/25 contract within 2 years and 6 months was particularly "challenging". The EY Review, cited in SEM-23-080, found that achieving consents and building project in 3.5 years to the start of a capacity delivery year was "unrealistic". Yet rather than allowing unrealistic developments to terminate, SEMC is proposing to extend their deadlines for delivery, entirely contrary to the ACER report and likely to further encourage less robust offers in the future if participants expect SEMC to take a similar approach going forward based on the precedent that has been set. The adverse selection that this causes between prudent and less-prudent participants is clearly not in the short-term or long-term interests of consumers of electricity with respect to price, quality, reliability and security of supply of electricity across the island of Ireland.

We note that the aforementioned EY Review recommended a more permissive approach for extensions to new build projects. However, this recommendation was in part based on a case study in which New Capacity was able to get a substantially higher price from terminating and re-entering an auction, and then inferring that it was the RA's hesitancy in granting extensions that was the cause of the termination. Crucially the EY Review did not consider any potential impact of its recommendation on the bidding behaviour of participants in future auctions, or how bids that sought to deliver in timelines that the review described as "unrealistic" were approved in the first instance.

4 Transparency, Competition and No Undue Discrimination

As per the consultation paper, the proposals will involve SEMC granting extensions on a case-by-case basis only when granting the extension is:

- consistent with the CMC Objectives,
- when the market participant has justified the request with robust evidence, and
- where the extension would otherwise be consistent with the SEM Committee's statutory duties.

These stipulations for when a request will be granted are not specified in J.5.2 which sets out the process for an extension to the Substantial Financial Completion date. In any legal drafting of the proposed modifications, these requirements for the granting of an extension to the Long Stop Date and the Capacity Quantity End Date should be explicitly written into the CMC.

In the interests of facilitating the objectives of competition, transparency, and no undue discriminations between participants, SEMC should make public the details of its decisions to grant such extensions, and in doing so should specify how its decision to grant an extension complied with the above requirements.

The extension of a CRM contract for a particular participant is relevant market information and should be published. Furthermore, it is important for investor confidence in the SEM for SEMC to be transparent in how it has arrived at such significant decisions, particularly when the criteria are relatively high-level and can be interpreted with a degree of ambiguity. For example, if SEMC determines that the delivery of the capacity is in the interests of consumers, then it may decide that for this reason alone a contract should be extended, regardless of whether the reasons for the delay were genuinely unavoidable and outside of the control of the participant, or whether the original implementation timelines were realistic.

Additionally, participants will want to understand what SEMC considers to be a justifiable reason and robust evidence for the award of an extension to a CRM contract. This is important to ensure that there is a competitive level playing field with no undue discrimination between participants, such that all participants know what is being deemed permissible with regards to granting extensions.

If SEMC are to proceed with the proposed modification, it will be important to set out how SEMC will arrive at and publicise their case-by-case decisions in a way that facilitates transparency, competition and no undue discrimination. At a minimum, Energia proposes that SEMC specifies the criteria for granting an extension in the CMC, and is required to publish detailed information, including supporting evidence, on the relevant decisions.

5 Conclusion

Energia is opposed to the proposed modifications on the basis that by changing the fundamental terms of concluded auctions they are retrospective in effect. The modifications are contrary to the ACER recommendation that penalties in capacity mechanisms incentivise participants to deliver new capacity in a timely manner. Finally, the modifications provide no assurance that extensions would be granted in a manner that facilitates transparency, competition, and no undue discrimination.