



Energy for
generations

ESB Generation and Trading's
Response to Proposal to Introduce
Intermediate Length Contracts
Consultation
(SEM-23-093)

21/12/2023

1. INTRODUCTION

ESB Generation and Trading (GT) welcomes the opportunity to respond to the Proposal to Introduce Intermediate Length Contracts Consultation (SEM-23-093).

The consultation sets out:

- the current arrangements in the SEM CRM and the key issues associated with those arrangements.
- arrangements in Other European CRMs; and
- proposed changes including the pros and cons.

We understand that the purpose of this consultation is to gather industry feedback on the creation of a new capacity market contract option which would allow generators to recover costs associated with the refurbishment of existing capacity. The purpose of such refurbishment would be to extend asset life and/or to reduce the carbon intensity of the existing dispatchable generation, and to create a route to market for new proposed assets that do not meet the current New Capacity Investment Threshold (NCIRT) of €300,000/De-rated MW.

While there is currently a mechanism within the Exception Application process for the existing generation assets to access a Unit Specific Price Cap (USPC), which includes Unavoidable Future Investment (UFI) costs, this mechanism does not provide access to a multi-year contract. This gives rise to cost recovery risk in a scenario where the unit does not achieve the multiple 1-year contracts required for full cost recovery.

We are supportive of this stakeholder engagement approach and recognise that this issue has been discussed within various modification proposals during Capacity Market Workshops, most notably the *CMC_12_23 Facilitation of Unit Specific Price Caps for Existing Capacity in Excess of the Auction Price Cap*. We trust you will find our comments to be both helpful and constructive.

2. EXECUTIVE SUMMARY

ESB GT believes the proposal to introduce Intermediate Length Contracts (ILCs) into the capacity market is appropriate in the context of an existing generation fleet consisting of predominantly older dispatchable generation. As recognised by the consultation, investments in existing capacity have the potential to improve system reliability, reduce emissions, extend the useful life of the existing assets while also providing a lower carbon alternative relative to new build OCGTs for an interim period whilst the SEM transitions to net zero-carbon.

Considering the broad spectrum of projects that may avail of this new option, and to ensure the potential for maximum participation and competition, we believe that a longer maximum contract length of at least five years and a lower investment threshold should be adopted.

Refurbishment options for generator units will vary greatly, including increasing performance and abatement of the currently unabated plant. As an example, a plant seeking to undertake a refurbishment to ensure its capability to operate on H₂ may require a contract of greater than 5 years to ensure its viability. Setting the contract duration too low and investment thresholds too high has the potential to limit the ability of market participants to participate in these amended auction process for ILCs.

Maintaining equity with between projects for the delivery of capacity under T-4 auctions is important. We therefore support the retention of 18 months Long Stop Date for all multi-year projects including ILCs. Projects which are in receipt of ILCs should similarly be able to avail of the reliefs afforded to new capacity in the case of project delays associated with Appeals to An Bord Pleanála, Judicial Reviews of An Bord Pleanála decision and other third-party delays as is allowed for under the Capacity Market Code (SEM-23-101 decision paper).

Additionally, projects in receipt of ILCs must be incentivise in their delivery through the application performance security and performance security requirements in the same way as new capacity projects.

ESB GT believes a review of CRM as a whole and its interaction with other support mechanisms needs to be undertaken to evaluate what supports are needed to incentivise further investment into low carbon technologies to support the transition to a net zero SEM. We welcome the inclusion of the review of the Capacity market and the new State aid application in the SEMC Forward Work Programme for 2023/24¹.

3. QUESTIONS

3.1. What is the appropriate maximum duration for the intermediate length contract?

ESB GT believes that intermediate length contracts should allow participants to recover the costs over a period that allows for broad and competitive participation in the capacity auction process. Existing units often have significant Net Going Forward Costs that need to be recovered regardless of the new investments. This may put refurbishing units into a disadvantaged position during the capacity auction

¹ [SEMC - Forward Work Programme Oct23 - Sept 24.pdf \(semcommittee.com\)](#)

if the maximum contract length is too short and therefore the unit's price is too high and potentially comparable with prices of new units that compete for the full 10-year contract.

Considering the current economic situation and high prices of all inputs needed to deliver successful refurbishment, we believe the appropriate maximum length of the intermediate length contracts should be at least 5 years, potentially even greater. This cost recovery timeline could allow units to be competitive in the capacity auction, putting downward pressure on auction clearing prices and creating an opportunity for the existing assets to extend their life and alleviate some of the security of supply issues.

This approach will help to strike a balance between the efficient utilisation of existing assets and the procurement of new capacity in delivering capacity at the lowest overall economic cost to consumers while ensuring security of supply is maintained.

3.2. What is the appropriate Intermediate Contract Investment Rate Threshold (ICRT) in €/MW_d for units to be eligible for the intermediate length contract?

Considering the main objective of the ILC is to allow for the refurbishment of the existing capacity we would caution against setting the ICRT too high. The existing generation capacity portfolio on the island of Ireland consists of units with a wide range of derated capacity from c.50 MW_d– 400 MW_d that may have the potential to be refurbished in a manner that would improve the de-rating factor of that asset and extend its lifespan but the requirements for each unit will vary greatly.

Considering the duration of the ICL is proposed as a maximum duration, ESB GT believes the ICRT should be set sufficiently low to allow participants to choose the appropriate contract length for their investment. This approach would also minimize any future calls for the introduction of more tailored contracts with specific lengths and investment rate thresholds. It is important that we create a stable regulatory environment and an appropriate investment signal for developers.

3.3. Is gaming a material concern? What approaches should be taken to prevent gaming of the new arrangements?

ESB GT understands the concerns that were included in the consultation paper regarding the need to monitor the actual spend versus ex-ante estimates for any refurbished units. As we have earlier suggested, a qualification regime that allows the maximum participation of units will result in the most efficient delivery of capacity ensuring that projects will only bid realistic costs to ensure competitiveness.

We would like to better understand what any new potential monitoring requirements could be if these are to be different from the existing monitoring of implementation plans for other projects. Publication of the monitoring guidance will allow any participant to structure the reporting requirements according

to these additional needs and will make the monitoring process more streamlined and allow for appropriate governance and compliance on both sides of the process.

3.4. What is the view on the proposed changes to the Existing Capacity Exception Application process and New Capacity Exception Application process?

While we support the use of the Exception Application process for the evaluation of the applications for the ILCs we are concerned about the capability of the current process to be extended to ILCs. The Exception Application process for the existing capacity is currently perceived by market participants as quite onerous and time consuming with a lack of a publicly available methodology to guide participants.

ESB GT understands the need for a thorough analysis of each application however, we believe the lack of a published methodology and guidance and the lack of publicly available information on Exceptions granted continues to create uncertainty for investors.

We believe that it is appropriate for the Regulatory Authorities to undergo a comprehensive review of the Exception Application process, especially if it will be used for the approval of the new intermediate contracts.

We also note the two recent modification proposals (CMC_20_23² and CMC_24_23³) which are seeking changes to the Exception Application Process Timelines within the auction calendar.

The last paragraph of part 5.4, “Changes to Exception Application processes”, in the consultation paper mentions potential need to demonstrate an intent to decarbonise in the future⁴. We would seek more information and clarification as to how the any required demonstration of intent is to be assessed, verified, and enforced in the application process.

3.5. Should Existing Capacity seeking a multi-year contract be required to submit implementation plans for consideration by the TSOs as a part of the Qualification process, and are the same milestones employed for New Capacity appropriate?

Appropriately detailed implementation plans should form part of the qualification documentation as for the New Capacity with appropriate assessment by the TSO and RAs. Given the potential for significant variation in the scope and nature of the refurbishment's projects ESB GT believes consideration should be given by the TSO, in consultation with individual project developers as to the milestones and requirements that are appropriate for the implementation plan for different projects.

² CMC_20_23 [Modification Proposal \(sem-o.com\)](#)

³ CMC_24_23 [Modification Proposal \(sem-o.com\)](#)

⁴ *When making an application for a multi-year contract, the applicant may need to demonstrate an intent to decarbonise aligning with energy strategies in Ireland and Northern Ireland.*

3.6. What is the appropriate length of the Long Stop Date for Existing Capacity seeking the intermediate length contract.

ESB GT believes the current long stop date of 18 months for multi-year new capacity contracts should be applied to refurbishing plants as well. Equitable provisions should be made to all projects with ILCs to be able to avail of the reliefs afforded to new capacity in the case of project delays associated with Appeals to An Bord Pleanála, Judicial Reviews of An Bord Pleanála decision and other third-party delays as is allowed for under the Capacity Market Code (SEM-23-101 decision paper).

We note that the consultation does not include any proposals regarding the impacts on the delivery of refurbishment on an existing contract that unit may be operating under, such as an allowance for secondary trading of the RO while the works are underway, outage planning, opt-out notifications, etc. Clarity on these matters should be provided for in the detailed design of the ILC process.

3.7. Should Existing Capacity with an intermediate length contract be subject to termination payments and performance security requirements?

ESB GT believes that termination payments and performance security requirements equivalent to those required for new capacity projects with 10-year contracts should apply to ILCs.

We note that the existing methodology for the calculation of the performance security requirements is calculated by reference to the level of new capacity being delivered and consideration should be given to how the calculation should be made for existing capacity that is being refurbished.

3.8. How could the design of intermediate length contracts promote investment in low carbon technologies?

The capacity market currently accommodates mostly fossil based thermal generation, demand side units and battery storage with a limited number of other technologies (hydro, wind). There are currently multiple other schemes on the island of Ireland designed to promote investment in renewable generation and renewable-enabling assets (RESS, O-RESS, LCIS and in the future LDES).

There is currently no scheme in the capacity market to incentivise investment either in new low CO₂ dispatchable generation or in transitioning existing fossil fuelled generation to low/CO₂ fuel. Securing net zero also needs zero carbon dispatchable generation, production, and seasonal storage of zero carbon fuel for this fleet of dispatchable generators.

Current auctions favour investment in natural gas/oil fuelled assets and do not reward/ incentivise any incremental, anticipatory investment for 'H₂ readiness' as has been noted above.

We believe that there is a need for such a financial incentive and that ILCs may present an opportunity for existing plant to transition to low carbon fuels through appropriate reinforcements.

Additionally, we include below a high-level overview of suggested support mechanisms needed for transition from natural gas to low carbon hydrogen.

Hydrogen to power

Transitioning existing gas plant to H₂ / H₂ blends.

The deployment of H₂ fuelled generation can be achieved through the refurbishment of existing generation assets. Based upon industry feedback it is suggested that the refurbishing capex is half that of new build⁵. The proposed access to ILC for existing gas-fired generation capacity to recover investments in plant to enable displacement of some or all of its natural gas consumption with renewable hydrogen is welcome, however, this is only one part of the chain. Hydrogen to power (whether 100% H₂ or a blend of H₂/CH₄) relies on the wider hydrogen economy and, in particular, depends on essential enabling infrastructure, i.e., renewable hydrogen production, hydrogen transport and hydrogen storage.

As well as the development of these ILCs we also note the need for the development of the growing hydrogen economy including investment in renewable hydrogen production, transport, and storage infrastructure which will support H₂ fuelled dispatchable generation.

New H₂ fuelled power generation.

To secure the first mover advantage in an infant industry it is also key that we look to secure the right contracts with effective durations longer than 10 years for new generation.

To provide confidence and increased certainty to developers as the technology itself matures, it is critical that viable routes to deployment are created, or an alternative market intervention, along the lines set out in GB may be required.

DESNZ is currently consulting on the need for and potential design of market intervention to support deployment of hydrogen to power.⁶ Research identified that first mover disadvantage and plant developers' inability to effectively manage risk in enabling infrastructure is potentially reducing investment certainty in hydrogen to power. DESNZ suggests that a variation of a Dispatchable Power Agreement (DPA)-style mechanism, a "Hydrogen to Power Business Model (H₂PBM)" could be suitable to mitigate the identified barriers to deployment and accelerate the deployment of hydrogen to power capacity.

A DPA-style mechanism providing an Availability Payment to incentivise higher cost, new H₂ fuelled power generation by providing a regular payment to de-risk investment should be explored in Irish

⁵ <https://assets.publishing.service.gov.uk/media/657a2eeb095987001295e072/hydrogen-to-power-market-intervention-need-and-options-report.pdf>

⁶ <https://www.gov.uk/government/consultations/hydrogen-to-power-market-intervention-need-and-design>

context. The payment would enable such plants to compete freely in power markets (excluding the CM whilst the plant is in receipt of a DPA) to maximise revenue opportunities and provide capacity and system services to support the system to be stable and secure.

Consequently, we believe the ILCs for the new capacity with a lower investment threshold are suitable for some low carbon technologies as per the proposed design. The same issue was recently discussed in the DESNZ Capacity Market Consultation in GB and the proposal for low carbon technologies contains 3-year contracts with potentially no capital expenditure threshold and also 9-year contracts with a threshold based on the average of the current 3-year and 15-year thresholds.

As mentioned above in question 4 (part 3.4) the consultation document mentions a potential need to demonstrate an intent to decarbonise in the future for the refurbishing plants. We believe it is in the interest of all investors and consumers to use the asset as long as possible and that may mean to invest into abatement solutions for the currently unabated plants.

4. CONCLUSION

ESB GT welcomes the proposals to introduce intermediate length contracts as a means to efficiently facilitate the extension of the operating life of existing generating units in order to maintain security of supply during the transition to a net zero SEM. It will help to minimise the need for longer term contracts for the new fossil fuelled generating units during the period that low carbon alternatives in the renewable and energy storage spaces are being realised. We believe that projects seeking ILCs should compete with and be incentivised equivalent to other multi-year projects delivering under the same auctions.

In addition to this initiative ESB GT believes there is a need to incentivise the transition to the new low carbon fuels during all stages to the development – from fuel production and storage to retrofitting the existing capacity to become low carbon fuel ready and building new low carbon fuel plants to replace the current fossil fuel units.