EPUKI Response to SEM-23-047 Consultation on Administered Scarcity Pricing Review

EP UK Investments (**EPUKI**) welcomes the opportunity to respond to this Consultation Paper. EPUKI strongly believes that reflecting scarcity in electricity prices is important to drive investment and retain Existing Capacity in the Single Electricity Market (**SEM**). However, the proposal to trigger Administrative Scarcity Pricing (**ASP**) more frequently without corresponding changes in the implications for generators will not be effective for incentivising availability at times of tight system margins and will not contribute to Security of Supply challenges in the SEM. EPUKI is therefore opposed to the suggested changes to the ASP methodology.

The proposal as drafted appears to be designed to result in significant negative consequences for generators who are unavailable without any corresponding incentivisation. The Consultation Paper notes that ASP has not been triggered during "*periods of tight margin and security of supply concerns"*, however it should be noted that many of the system events over the past 24-36 months have not been driven by low availability of generation but rather by constraints on the transmission network. It is thus questionable whether further incentivising reliability would have made any difference in such cases. Without a detailed Impact Assessment, it is unclear how the Regulatory Authorities (**RAs**) have evaluated the implications of this proposal and the corresponding impact on consumers, generators and suppliers. To propose a change such as this without an Impact Assessment is inappropriate. EPUKI is of the view that the high-level proposal, and the options presented in the Consultation Paper constitute a further shift of Security of Supply responsibility from the Transmission System Operators (**TSO**) onto Participants. EPUKI believes that these proposals should be subjected to a Regulatory Impact Assessment before being progressed any further.

Reliability Option Strike Price

EPUKI believes that the true value of scarcity is distorted as a result of the Reliability Option Strike Price (**ROSP**). Where the market price goes above the ROSP in any trading period then generators who hold capacity contracts are obligated to pay Difference Charges in that trading period. In theory, this limitation is applicable only to the volume of de-rated capacity which is contracted through the Capacity Market and subject to the load following factor. Any excess capacity may be sold at a rate above the ROSP without incurring Difference Charges. However, due to the current load following factors, as determined by EirGrid, capacity holders have very little excess capacity to sell to the market. This inherently limits generators' ability to benefit from scarcity which is an ineffective signal for investment in existing or new capacity. In practice the ROSP has acted as a de-facto cap on the pricing in the market.

This means that the incentive created by the ASP is downside only, where a unit which is unavailable will be required to pay back the difference between the ASP and the ROSP. Triggering ASP more frequently would represent a significant risk for generators, with little discernible upside. As a result, generators would be required to price additional risk into their pricing in all markets resulting in higher prices for the consumer, particularly in the shorter term. Additionally, the value of the CRM contracts would be seen to be reduced due to the risk of RO penalties, and it is likely that this would also be priced into the bidding behaviour of new and existing participants. The consequences of this are likely to be long term higher CRM clearing prices affecting consumers and suppliers. As stated above, this would have little impact on system events, which are primarily driven by constraints, but would serve as an exit signal for Existing Capacity in the SEM.

Because generators incur Difference Charges for energy sold above the ROSP, market prices rarely (if ever) clear above the ROSP, even if the value of energy during periods of scarcity is greater than this.

Because the ROSP takes account of fuel prices only, it will never reflect scarcity in how it is calculated. While the ROSP may seem to protect consumers from higher prices, it actually has unintended consequences which arise during scarcity events. The existence of the ROSP often results in system stress events being aggravated due to scarcity pricing in other markets. For example, the lack of a similar mechanism in Great Britain (**GB**), means that during periods of low wind, the interconnectors are often exporting to benefit from higher prices in GB. The artificial price dampening caused by the ROSP prevents the SEM from providing a competitive price signal which results in an underutilisation of resources in the SEM. This issue will likely worsen following the scheduled connection of new interconnection to GB and Europe, as European markets generally do not have a similar ROSP mechanism.

Finally, we believe that greater upside incentive would be more likely to encourage demand response during periods where margins are tight. If variable demand is not responding to existing market signals it suggests that these signals need to be strengthen in order to encourage a response. The ROSP caps the revenue available to demand side units and thus does not provide adequate compensation to result in a demand reduction.

Based on the above, EPUKI requests that the SEM Committee (**SEMC**) review the ROSP in the context of scarcity pricing and consider the impact that ROSP will have on Security of Supply in the medium and long-term. In particular, the interaction between the ROSP and ASP should be carefully considered in the context of reliability incentives and medium to long-term signals for Existing and New Capacity.

Security of Supply Responsibility

EPUKI believes that the proposals in this Consultation will further shift responsibility for Security of Supply from the TSOs to market Participants. Many of the system events in the past 24-36 months have been driven by network constraints, rather than generation being unavailable. It is evident that much of the scarcity which exists in the SEM is locational, rather than system wide. Locational scarcities would be more efficiently and robustly addressed through network development and infrastructure. This approach is also more aligned with the design of the SEM itself, as a single all-island system rather than separate jurisdictions with a single connection.

This shift in responsibility is evident in the Options presented in the Consultation Paper. For example, Option 2a proposes to trigger ASP if scarcity occurs in either jurisdiction to account for constraints between Ireland and Northern Ireland. This would expose generators in Northern Ireland to significant risk of inflated Difference Charges should they trip or become unavailable. EPUKI believes that this is completely inappropriate given that the impact of constraints is a direct result of the TSOs failing to deliver the North-South Interconnector in a timely manner. The North-South Interconnector was originally scheduled for completion in 2017. This would have significantly reduced the impact of interjurisdictional constraints on Security of Supply. It is unacceptable that under this proposal it is generators who are expected to bear the responsibility of this delay through greater risk exposure. It is unclear whether the reserve requirements to trigger ASP are set at an appropriate level in NI and ROI under this proposal, which would also need to be reviewed in detail.

Option 2b presents similar issues, where market Participants will be exposed to Difference Charges at ASP due to the constraints which are entirely the responsibility of the TSO to manage and resolve. EPUKI believes that there should be stronger incentive on the TSO to develop the network and ensure Security of Supply in accordance with its statutory and regulatory obligations.

It is procedurally unfair to penalise generators based on network quality which is the responsibility of the TSO. EPUKI notes that an asymmetry of information exists whereby the TSOs have a full overview

of the network, flows, and planned investment and reinforcement. Any changes to the ASP driven by constraints would be exposing Participants to Difference Charges based on signals which they do not have vision of.

Secondary Trading

EPUKI believes that any changes to the application of ASP would be inappropriate until robust and reasonable secondary trading arrangements are in place. It is noted that two Capacity Market Code modifications related to secondary trading have been approved by the SEMC but have not yet been implemented by the TSO. The first of these modifications, CMC_11_21, enabled Participants to secondary trade above a unit's de-rated capacity. This modification was approved by the SEMC in September 2021 but has not been implemented by the TSO. The implementation date for this modification has been pushed out several times to prioritise TSO modifications.

A second modification, CMC_09_22, which would provide greater transparency to Participants in relation to secondary trading, making it a more viable operation, was approved in September 2022 and has also not yet been implemented.

Secondary trading can ensure that alternative capacity is sourced and in place when a unit is unavailable. It is inequitable and procedurally unfair to increase the burden and risk on generators in general, and this is worsened when secondary trading improvements are still unavailable two years after being approved.

Load Following Obligation

EPUKI refutes the SEMC position that "*high prices triggered by ASP can also serve as an investment signal for resources who do not hold ROs, or to a limited extent for RO holders insofar as it relates to the portion of their capacity which is not obligated under the RO".*

It is not realistic that New Capacity can be delivered or retained in the SEM without having some form of capacity contract. In recent years there has been a significant number of terminations of Awarded Capacity projects, and closure of Existing Capacity in the SEM. This is demonstrative of the challenging economic environment for projects which have secured a capacity contract. If it is very challenging for contracted generation to deliver in the SEM, EPUKI expects it would be impossible for projects to remain economically viable without a capacity contract in place.

Furthermore, ASP prices are available only through the BM. It is unrealistic to expect a developer to create a successful business case for new investment based only on BM prices. It is further unclear whether scarcity can be included in ex-ante bids under the Bidding Code of Practice (**BCOP**). The economic benefit of high prices is further dampened due to the ROSP as outlined above.

As noted above, capacity contribution obligations under an RO are dictated by the Product Load Following Factors (**PLFF**) as determined by the TSOs and approved by the RAs. PLFFs from October 2023 to March 2024 are 0.973. This effectively means that generators have little to no headroom above their RO obligations to benefit from high ASP prices as suggested by the Consultation Paper.

Impact Assessment

EPUKI notes that the Consultation Paper does not include any overview of expected regulatory impact on the market or economic impact on Participants. EPUKI considers such a review necessary to ensure robustness in decision making and procedural fairness. Failure to undertake a detailed review of these proposals is highly likely to lead to unintended consequences and negative market signals in the medium to long-term which may worsen Security of Supply concerns.