



Energy for
generations

ESB Generation and Trading's
Response to *Amendments to the
Duration of the Directed Contracts
Primary Subscription Window*
(SEM-23-015) consultation.

03/03/2023

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1. INTRODUCTION

ESB Generation and Trading (GT) welcome the opportunity to respond to the consultation on *Amendments to the Duration of the Directed Contracts Primary Subscription Window* (SEM-23-015). We recognise that the purpose of the paper is to seek industry views on two specific proposed amendments and have addressed the two related questions in the first section of our response. In addition, our response also includes a section on current market conditions within the SEM and consideration of the regulatory principles relevant to Directed Contracts (DCs).

2. PROPOSED ENDURING AMENDMENTS TO THE DIRECTED CONTRACT PROCESS

2.1 Response to Q1: Do you agree that the proposed amendments (increase from 3 to 6) to the duration of the DC Primary Subscription Window should become an enduring arrangement?

ESB GT do not support the proposed amendment to increase the DC Primary Subscription Window to 6 days, for the following reasons:

- a. The increase in the primary subscription window, from 3 to 6 days, was introduced specifically to address the following specific, **temporary** (albeit challenging) market conditions relating to extreme price volatility (gas). However, now that the market has settled there is no longer a requirement for the 6-day window.
- b. The 6 days increases **collateral risk** for ESB GT. Our experience from the recent 6 days DC rounds indicate that suppliers are less likely to post credit cover than in the original 3-day window. Reducing to 3 days is expected to encourage suppliers to tighten their processes.
- c. Increased risks due to commodity price exposure – As the RAs are unable to update the DC model during the subscription window period to more accurately reflect commodity prices during the period, ESB GT carries a **disproportionate risk** as it is locked into the DC market concentration model pricing formula and therefore exposed to changes in commodity prices during this time. In the case where the RAs decide to amend the Primary Subscription Window to 6 days ESB GT request that the DC model is updated each day (or at least every 2 days) during the period.
- d. Increasing the Primary Subscription Window by 3 days would effectively double **administrative burden associated** with Directed Contract regulatory intervention for ESB GT. Given the forecast reduction in Directed Contract quantities (see below), we argue that the additional

burden associated with the proposed increase in the Primary Subscription Window cannot be justified.

ESB GT do not support the proposed amendment to increase the DC Primary Subscription Window from 3 days to 6 days.

Decline in Directed Contract volumes

Table 1 below provides details of the Directed Contract volumes sold over the past seven years and shows how the quantities have declined by over 50% during this time. The reason for this downward trend in Directed Contract quantities is that the overall volumes of ‘competitive’¹ capacity used in the market concentration model are continuing to decrease. This is due the increase in renewable generation which has the effect of reducing the proportion of conventional generation considered competitive within the DC market concentration model.

Table 1: Directed Contract volumes (TWh)						
2016	2017	2018	2019	2020	2021	2022
4.4	4.3	5.3	5.1	4.2	3.2	2.3

Source: ESB GT

In the coming years the proportions of conventional generation are expected to further decline in line with the forecast increase in renewable generation – In 2022 approx. 36%² of electricity was generated from intermittent renewable energy and this will need to increase to 80% in order to achieve the Climate Action Plan target by 2030³. As the volumes of renewable generation increase there will be a commensurate decrease in competitive capacity, consequently the volumes of Directed Contracts that will be required to reach the RA’s specified Herfindahl Hirschman Index (HHI) level of 1,150 are expected to decline proportionality.

RESS support structure

ESB GT also consider that there is an increasing need to reflect the two-way CfD nature of RESS support within the market concentration model. Renewable generation projects supported through RESS are not competitive as they do not have an incentive to influence the market price. This is

¹ Capacity that is relevant to competition – is calculated hourly for the various generation owners based on the cost of each generation owner’s units. In a given hour, a unit’s capacity is considered potentially competitive so long as its cost is less than or equal to the DAM Price * (1.05).

² EirGrid website: [System-and-Renewable-Data-Summary-Report.xlsx \(live.com\)](https://www.eirgrid.ie/system-and-renewable-data-summary-report)

³ [gov.ie - Climate Action Plan 2021 - Securing Our Future \(www.gov.ie\)](https://www.gov.ie/publications-and-statistics/publication/climate-action-plan-2021-securing-our-future)

because any effort to influence market prices would result in either a reduction level of support from the PSO or an increase in the amount they would be required to pay back to the PSO.

ESB GT proposes that all RESS supported generation should be atomised within the market concentration model on the basis that they are not incentivised to influence market prices as has previously been the case of other PSO supported generation, i.e. West Offaly, Lough Ree and Edenderry.

ESB GT propose that all RESS supported generation should be atomised with the market concentration model

Supplemental Subscription Window

The intention of the Supplemental Subscription Window is to allow suppliers an additional day to purchase any volumes that were not taken in the Primary Subscription Window. However, in view of the expected reduction in Directed Contract volumes ESB GT question whether the Supplemental Subscription Window should continue. In our view the inclusion of the additional day places additional **disproportionate risk** on ESB GT. As previously mentioned ESB GT remain locked into the DC model pricing formula for the complete period of the DC round and therefore exposed to changes in commodity prices during this time. Since existing retailers have had the opportunity to purchase Directed Contracts in the Primary Subscription Window and in view of the declining volumes we request that the Supplemental Subscription Window is removed as it is no longer necessary.

ESB GT request removal of the Supplemental Subscription Window.

However, in the case where the RAs decide to continue to include the Supplemental Subscription Window, ESB GT suggest that it would be more equitable to also offer the Directed Contracts available in the supplemental window to new players. Since Directed Contracts have not been offered to new players in the past they are not included in the calculation of proportion, therefore offering new players the opportunity to purchase Directed Contracts via the supplemental window could offer a more equitable / inclusive proposition, whilst also recognising that the new players will also need to sign up to the Financial Energy Master Agreement (FEMA) with ESB GT including the necessary credit terms and conditions.

Residual volumes

According to the existing Market Concentration Model methodology, as set out in SEM-17-081⁴ a fixed fraction is used to allocate the Directed Contract quantities in the first round that a product is offered and in subsequent rounds up to the penultimate round, previous volumes that have been sold are deducted from the annual total in that round and the balance is then multiplied by the fixed fraction. In the final round, all the previous volumes sold are deducted from the annual total determined, unless the volumes in the previous rounds for a particular product add up to more than the annual volume in the last round, in which case the volumes for that product will be set to zero.

In our view the diminished volumes of Directed Contracts currently offered no longer justify the administrative complexity associated with implementing the Directed Contract quantity allocation described above. ESB GT request that in the instance where volumes remain following a DC Round, that these volumes are not carried forward as this practice serves to add to the administrative burden and also extends the duration of the volume and collateral risk for the company.

ESB GT request that any volumes remaining after a DC round are not carried forward into subsequent DC rounds.

2.2 Response to Q2: Do you agree that market participants should be obliged to participate during each day of the Primary Subscription Window in a given DC Round, i.e., suppliers would be eligible to purchase only 1/6th of their allocated volumes during each day of the six-day Primary Subscription Window?

ESB GT are supportive of the proposal to obligate suppliers to participate during each day of the Primary Subscription Window in a given DC Round, but emphasise this should be over 3 days rather than 6 days. We recognise that this proposal could address concerns previously expressed regarding ESB GT's exposure to changes in commodity prices over the subscription window and therefore reduces the volume risk, which assists in restoring the imbalance in the risk carried by ESB GT versus suppliers, especially on the last day.

Whilst we recognise that this proposal will take an element of flexibility away from suppliers, we also draw attention to the need for Directed Contracts as regulatory intervention to be fair to parties on either side of the trade.

⁴ [SEM-17-081 DC Implementation Decision for I-SEM.PDF](#)

We also caution against spreading the volumes over 6 days as this could make the Directed Contracts administratively very difficult for small suppliers, placing an additional **administrative burden** on them and discouraging them from engaging in the process. Similarly, the management of such small volumes would also increase the **administrative burden** for ESB GT.

3. CURRENT MARKET CONDITIONS IN THE SEM

As previously stated in the ESB response SEM-20-045⁵, we request that a full review of the market evidence supporting the need for Directed Contracts is conducted. We specifically refer to the SEMC Information paper⁶, which was published following this consultation and states:

In light of responses received, the SEM Committee now intends publishing data on market power and liquidity in the SEM (publication of such data to commence prior to the end of 2021), and to use such data to: - facilitate a decision by the SEM Committee as regards the existing market power framework; - consider any further potential regulatory interventions in the forward market; and - consider whether any regulatory investigations are required.

We maintain the view that the application of the existing Directed Contract obligation is now disproportionate in its effect on ESB GT as the sole provider, we therefore consider that a comprehensive review of this regulatory intervention is long overdue.

Request that the RAs conduct a full review of the market evidence supporting the need for Directed Contracts.

3.1 Market Share – Installed capacity

Table 2 provides details of installed capacity in the SEM.

Table 2: Installed capacity (2022) incl. wind and interconnection								
Year	Aughinish	Bord Gais	EP	ESB	IC	Other IPP	SSE	Viridian
2021	1.1%	3.5%	7.4%	30.1%	6.2%	29.0%	14.9%	7.8%
2022	1.0%	3.3%	7.0%	28.5%	5.8%	33.5%	13.9%	7.0%

Source: System Operators and ESB

⁵ Market Power and Liquidity Discussion Paper, SEM Committee, 7 July 2020

⁶ [SEM-21-007 Market Power and Liquidity Information Paper.pdf](#)

Since Directed Contracts were introduced the market has changed substantially - in 2022 ESB GT had 28.5% of installed capacity. Since all new capacity qualifies through the competitive capacity auction process ESB GT argue that the exclusive obligation on the company to offer Directed Contracts is unfair, as it effectively penalises ESB GT for delivering competitive capacity to the market. Therefore, in the case where the RAs decide to continue with the Directed Contract regulatory intervention, we consider that it would be fairer and more equitable to spread the obligation proportionately amongst other large generator participants.

3.2 Market share – Commercial volumes

Table 3 provides details of ESB GT share of volumes sold in the ex-ante markets - both the Day Ahead (DA) market and also, the DA and Intraday (IDA)⁷ markets.

Year	DA	DA & IDA
2021	30.2%	30.8%
2022	25.4%	25.2%

* Half the volumes of the 2 ESB JV wind farms were included in ESB GT share values.

Source: SEMO and ESB

Again, the data indicates that ESB’s generation market share has fallen significantly since Directed Contracts were introduced the market – with a market share of 25.4% this is below any reasonable threshold where market power could be presumed. This is at a time when following the Covid-19 pandemic two IPP plants have undergone prolonged outages due to maintenance requirements and a high degree of volatility in the wholesale gas market has resulted in coal plants coming into merit. A situation which was compounded by low wind generation in 2021 and sustained demand growth throughout the period. Therefore, in view of the current market composition and accounting for the prevailing conditions, we believe that historic concerns about ESB’s market power in the generation market are no longer considered relevant.

4. REGULATORY PRINCIPLES RELEVANT TO DIRECTED CONTRACTS

ESB GT recognise and support the need for regulatory principles to ensure a level playing field, necessity, proportionality, transparency and non-discrimination. These principles are derived from EU

⁷ Incl. Intraday 1, Intraday 2 & Intraday 3

law, and in particular the Electricity Directive (which is and will remain applicable in both Ireland and – by virtue of the Withdrawal Agreement – in Northern Ireland).

We note that the consultation paper states that Directed Contracts (DCs) are part of the Regulatory Authorities' (RAs; i.e. CRU and UREGNI) market power mitigation strategy to ensure the benefits associated with the SEM are not undermined by abuse of market power by incumbent generators.

Whilst we recognise that in the past the SEMC were cautious about removing the Directed Contract regulatory intervention, particularly when the new ISEM market design was introduced in 2017, we now question the validity of this intervention. Six years on the ISEM has a history of successful operation and evidence to indicate that the market design and regulatory features such as Bidding Code of Practice (BCoP) have been effective in promoting competitive outcomes. In addition, as REMIT⁸ places legal requirement on all market participants to not manipulate the market, generators withholding capacity would breach this regulation.

Therefore, in light of the updated market evidence presented in the previous section and in recognition of the success of the ISEM market design, we question whether the continued imposition of Directed Contracts on ESB GT as the sole provider, can be considered to align with the regulatory principles listed below and consequently justified in the today's market.

Necessity: Recognising that the ISEM has demonstrated effectiveness in promoting competitive outcomes, and in view of the market evidence indicating that ESB GT does not have material market power, we question the basis for the obligation on ESB GT as the sole provider of Directed Contracts.

We draw attention to observations in our previous response to SEM-20-045⁹ where we mention that since the introduction of the new ISEM market design, SEMC has yet to present evidence to explain why the existing market measures to promote competition as well as the ex-post sanctions are insufficient in delivering the market power mitigation strategy, or why there is a continued requirement for Directed Contracts. We therefore consider that this regulatory intervention can no longer be deemed necessary or relevant to achieving the stated objective.

Proportionality: Directed Contracts place a disproportionate risk on ESB by comparison to the benefit afforded to suppliers.

⁸ [Regulation \(EU\) No 1227/2011 of the European Parliament and of the Council of 25 October 2011 on wholesale energy market integrity and transparency relevance \(europa.eu\)](#)

⁹ Market Power and Liquidity Discussion Paper, SEM Committee, 7 July 2020

Transparency: Model underpinning Directed Contracts lacks transparency in how the parameters have been designed and developed and it is also inflexible in responding to new circumstances that impact market pricing.

Non-discrimination: We consider the exclusive application of the regulatory intervention on ESB GT to be disproportionate and unfair discrimination. Therefore, in the case where the RAs consider continuing to apply the regulatory intervention, we request that the obligation to offer Directed Contracts is shared with other generators.

5. CONCLUSION

Fundamentally, ESB GT do not support the continued imposition of the Directed Contract regulatory intervention on ESB GT as the sole provider. We call upon the RAs to conduct a full evidence-based review of the market and to engage with industry to assess the requirement for Directed Contracts.

In the interim and with specific reference to this consultation ESB GT do not agree that the proposed amendments (increase from 3 to 6) to the duration of the DC Primary Subscription Window should become an enduring arrangement. We request that the Primary Subscription Window remains 3 days and that the Supplemental Subscription Window is removed. We also request that any volumes remaining after a DC round are not carried forward into subsequent DC rounds.

ESB GT are supportive of the proposal to obligate suppliers to participate during each day of the Primary Subscription Window, again as an interim solution, and emphasise that this window should remain 3 days.