

**NIE Energy Limited
Power Procurement Business (PPB)**

**Fixed Cost of a Best New Entrant Peaking
Plant
&
Capacity Requirement
for the Calendar Year 2011**

Consultation Paper

SEM-10-034

Response by NIE Energy (PPB)

30 June 2010.



Introduction

NIE Energy – Power Procurement Business (“PPB”) welcomes the opportunity to respond to the consultation paper on the Fixed Cost of a Best New Entrant Peaking Plant and the Capacity Requirement for the Calendar Year 2011.

General Comments

PPB is concerned at the change in the proposed Annual Capacity Payments Sum for 2010 which is approximately 2.2% lower than the amount for 2010. The reduction arises from a reduction in the proposed BNE Peaker Cost and again highlights the volatility of the CPM which was to be a more stable element of the market pricing.

It should also be recognised that in addition to this proposed reduction, capacity payments to generators will be further diluted in 2010 as a result of the overall increase in capacity (renewables and CCGTs at Aghada and Whitegate, offset by some closures/reductions).

While it is difficult to challenge many of the individual elements of the determination of the BNE price, there are a number of elements that we believe serve to understate the BNE price that we comment on in the Specific Comments section below.

In addition there are two key factors we believe result in the further understatement of the BNE price and which should be reflected in the final determination.

Foreign Exchange Rates

The first is the exchange rate used to convert all the costs to Euros. The analysis by CEPA was concluded in May 2010 and we note from Section 7.1 of their paper that they used a €/£ exchange rate of 1.1341 corresponding to the market rates on 14 April 2010 and although it is not stated, we assume all exchange rates reflect the rates prevailing on 14 April 2010. The Dollar has strengthened against both the Euro and Sterling since April and similarly Sterling has strengthened against the Euro (currently c €1.235/£). The cost of equipment is generally dollar based (as illustrated in figure 3.2 of the CEPA report) and hence the strengthening dollar will result in an effective increase in equipment costs (in both Euros and Sterling). We believe the determination of the BNE costs should use the most recent foreign exchange rates.

The reference date for the exchange rate is also an issue for the actual payments since the actual capacity revenue for Northern Ireland generators is influenced by the Annual Capacity Exchange Rate determined by SEMO. In the past this exchange rate has been determined at a different time distorting CPM revenues for NI generators. A more co-ordinated and consistent approach is needed in relation to the application of such exchange rates.

TLAFs

The RAs published a consultation paper (SEM-10-039) setting out their minded decision to adopt a uniform TLAF of 0.98 from October 2010. As a TLAF of 0.98 reduces the effective capacity of the BNE generator, if Uniform TLAFs are adopted, the determination of the annualised BNE Peaker cost should be determined using the loss adjusted capacity of 186.3MW (i.e. 190.1MW * 0.98).

Specific Comments

Initial Fuel Working Capital

In our response last year we commented that the distillate only option would need to hold fuel in excess of the obligation to hold 3 days of strategic fuel stocks to ensure that actual despatch does not result in the generator breaching its obligations in relation to its strategic stocking. This was recognised in the decision paper (SEM-09-089) which increased the cost to reflect the need to stock a further half days worth of fuel. We are surprised the consultation paper for 2011 reverts to 3 days of stocks.

Recurring Costs

The paper quotes gas transportation tariffs for Northern Ireland for 2010/11. These are not the final rates and represent an estimate published in August 2009. The actual tariff for 2010/11 is likely to be published in August 2010.

As we have commented in previous years, it is not clear that basing the gas capacity requirement on 4 hours operation is prudent. This is particularly relevant as gas nominations cannot be profiled and must be provided in a flat 1/24th profile. Hence it would be impossible to deliver the gas to operate the plant at short notice without either incurring gas balancing penalty charges or being restricted. There have also been occasions where peaking plant have operated for longer than 4 hours and we would suggest the gas capacity requirement should be based on a 12 hour operational requirement.

In line with our previous point in relation to the fuel stocking requirements for the distillate only option, the recurring fuel working capital cost would also be higher.

Ancillary Service revenues

The Ancillary Service revenue is over-stated.

Firstly there is an inconsistency in the expected running regimes. Section 10 states that the units are never scheduled in any of the 25 iterations, yet in Section 11, the assumption is that the units run for 5% of the year. While there may be some level of running as a result of constrained operation, 5% amounts to 438 hours. The determination on gas transportation charges assumes a maximum 4 hours of operation on a peak day. This implies that the BNE plant will be constrained on for a minimum of 110 days in any year. We do not consider this to be plausible assumption.

Secondly, the calculations of AS Revenue shown in Table 11.1 and those shown in Table 6.1 of the CEPA paper show the same net revenue but make two very different assumptions. As noted above, the consultation paper assumes the unit runs for 5% of the hours at a 60% load factor and determines POR, SOR, TOR revenues on that basis. The CEPA paper concludes in section 6.2 that the only relevant AS revenue is replacement reserve (presumably de-synchronised). The calculation in Table 11.1 seems to use an overall availability of 95%. On that basis the maximum replacement reserve that the BNE unit can earn is €806,826 (i.e. $190.1 * 8760 * 0.95 * €0.51/\text{MWh}$), before any GPI penalties are applied. Hence the €920k used in the determination of the BNE is overstates the HAS revenues the BNE plant will earn.

Capacity Requirement for 2011

We note the caveats in relation to the demand forecasts and agree that they should be re-assessed closer to the date of the final decision (as we also have proposed for foreign exchange rates).

As we have noted in our previous responses, we continue to disagree with the use of “target” forced outage rates and believe that actual rates (averaged over a number of years) should be used which more accurately reflects the risk to security of supply.

The treatment of wind remains unclear. Our interpretation of section 13.3.6 is that the wind is deducted off the load to produce a demand net of wind that is then used in CREEP against the generation to determine the LOLE and then “reference” plant is added to reach the target LOLE. A capacity credit for wind is then added back to determine the overall capacity requirement. If our understanding of the process is correct then it will understate the capacity requirement since it is in effect assuming fixed availability of wind on the basis of the profile. This is clearly not the case and a higher capacity requirement would be required to cover this risk.