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Dear James, Andrew

RE: Principles of Dispatch and the Design of the Market Schedule in the Trading and Settlement Code

As you are in doubt aware, there are a number of developments in Ireland and Europe which will drive change in the Single Electricity Market (SEM) in the coming years. Amongst these changes are greater levels of intermittent generation and interconnection on the island of Ireland as well as European requirements for regional integration. In attempting to address market anomalies which may arise as a result of greater levels of intermittent generation, Bord Gáis Energy (BG Energy) suggests that this consultation, although vast in application, is too narrow in focus.

The proposed changes outlined in the Regulatory Authorities (RAs) paper would represent significant changes to the fundamental structure of the SEM, as provided for in High Level Design of the market. The provisions of firm access rights and an unconstrained market schedule are two fundamental elements of the market and how generating parties are compensated in the energy market. Changing these aspects of the market will create huge uncertainty and risk in the market and to its participants. This will act to undermine investment and financial arrangements supporting these investments, which will in-turn jeopardise the achievement of the islands' renewable targets and increase costs to customers both in the short-term and long-term.

1. Construction of the Market Schedule and Allocation of IMRs behind Constraints

The underlying objective behind the proposals to align the market schedule (MS) and dispatch schedule (DS) and to allocate infra-marginal rents (IMR) behind constraints

is to reduce costs, predominantly the costs of constraints, levied on customers. BG Energy agrees with the broad principle that constraint costs should be minimised but also that the costs of constraints should be levied on those who are giving rise to the cost. However, the market schedule was initially designed to provide transparency to the market. Attempting to synchronise the MS and DS without greater transparency around the DS process and rules would be a retrograde step for the market. In this regard, BG Energy would not support any changes to the MS until such time as there is more clarity on the composition of the DS.

Furthermore, the costs of constraints can be managed under the current market arrangements without creating the level of risk and uncertainty associated with the changes proposed by the RAs. A large proportion of the expected increase in constraint costs will be caused by the lag in grid development. This lag and associated cost could be better managed through a ‘contractual framework’ between the connecting party and the party responsible for the development of the grid, the System Operators (SOs). This type of ‘contractual framework’ would seek to incentivise the timely roll-out of the grid but also the timely development of the generation assets by investors. In so doing, it will reduce the costs to customers by ultimately levying the cost of investment and development on those parties who can best manage the risk.

It is our understanding that a key reason for the current difference in the MS and DS is the requirement for reserve rather than plant characteristics or firm access availability. The provision of reserves is a value-added service to the security of the system and should therefore be compensated accordingly. Similarly, the technical characteristics of certain efficient and flexible plant provide value, particularly in facilitating intermittent generation. The current market arrangements do not effectively reward/compensate these “ancillary services” and the RAs proposals in relation to the alignment of the MS and DS and the dismissal of firmness will erode their value completely from the market. This will in-turn incentivise investment in cheap, ‘quick to develop’ plant and the associated investors will not provide the required ancillary services as they will not be adequately compensated for the value that they provides.

To avoid this scenario and the creation of greater congestion by the uncoordinated development of cheap generation plant, a robust market for ancillary services must be developed and parties who do not technically provide value to the system but whom

claim value through availability should be penalised financially. This will act to incentivise exit and/or incentivise the entry of technically efficient plant. Combined, these proposals will act to more closely align the MS and DS without initiating radical change to the SEM design.

2. Development of a Material Level of Harm Framework

In proposing the application of a ‘material level of harm’, the RAs are essentially developing a mechanism by which the SEM will be assessed and evaluated. The scale of such a review will require a ‘framework’ through which the performance and effectiveness of the SEM can be measured against the core objectives of the market. The provision of such a framework seems sensible, once it can and is applied consistently across a larger consultation and review of the SEM.

We do not support the proposed favoured Option 1 as its potential introduction would do unprecedented harm to the market.

The core objectives of the SEM as outlined in the founding documentation of the market are to create a ‘competitive, sustainable and reliable energy market’ by providing security of supply, stability, practicality, equity and efficiency. The legislation underpinning the SEM placed firm obligations on the RAs in relation to: a) protecting the interests of customers, b) ensuring authorised persons can finance their activities, c) promoting the use of energy from renewable sources and d) having regard for the environment. These objectives are not always mutually exclusive particularly when considered against short-term and long-term timeframes.

Recognising these plethora of objectives and the need to balance them in the short-term and long-term, a ‘material level of harm framework’ will need to agree weightings for the individual objectives at the outset and to include both quantitative and qualitative inputs. To determine whether a ‘competitive, sustainable and reliable energy market’ has indeed been achieved the framework will need to examine amongst other areas; whether the market is providing energy at comparable prices; if there is sufficient liquidity in the wholesale market to induce competitiveness; whether costs such as constraints, imbalance charges, PSO levies and generator performance incentives are providing value for money; whether stability and choice is provided to customers; is the security and stability of the system being upheld and whether investors can source and sustain financing for their investments.

3. Least Cost Dispatch and Priority Dispatch

BG Energy supports the proposed decision on least cost dispatch. The principle of ‘minimising production costs’ in the DS is logical and sensible from an economic standpoint.

However, it is not clear from the paper the avenue for **price making** renewable to achieve priority dispatch. Clarity is also required here.

BG Energy supports the RAs proposed decision on affording renewable priority dispatch and agrees it should be consistent with the legislative requirements of the RES Directive. We also support the proposed hierarchy with respect to wind, hydro, peat and CHP.

4. Grid Code Compliance and Provision of Information by TSOs

BG Energy agrees that grid code compliance is an important element of ensuring optimum dispatch of plant on the system and would highlight the following additional points:

- Incentives on interconnector performance should be as equally strong as incentives on generation units
- Strong incentives should be placed on the SOs relating to the performance of electrical grids
- Grid code compliant generators should not be penalised because of non-compliant generators. We understand that approximately 500MW of renewable plant that cannot be constrained /curtailed, and as a result neighbouring dispatchable plant is being turned down to meet system needs. This is an unacceptable principle and reality in the market.
- The revenues from any new penalties introduced on generators should be distributed to compliant parties. This means the penalty could be halved yet remain equally as strong.

Notwithstanding this, the Grid Code itself does need to reflect and to be cognisant of actual technical capabilities of generation assets. Accordingly, the Grid Code needs to be reviewed and changed such that the provisions in the Code can actually be achieved and complied with by all units.

With respect to the provision of information by the SOs, adequate, accurate and timely information from the SOs is needed if generators are to manage the technical and financial uncertainty associated with high levels of intermittent generation and interconnection. EirGrid's report on the 'Facilitation of Renewables' was a very useful and an insightful piece of work as a starting point for stakeholders to understand the extent of the system changes needed to support our renewable targets. Following on from this, clarity and updates on the SOs work-plans and analysis of constraints, curtailments and losses should be provided on an ongoing basis to the market on a quarterly basis.

Also, the quarterly TSO report on curtailment referred to in the paper should be made available to all industry participants and should be published monthly.

5. Tie-Break

BG Energy supports the RAs proposal to de-load plant in a tie-break situation on a pro-rata basis. Not only is it practical and easy to implement, it would in BG Energy's view, be more consistent with the other supports and incentives offered in the market to renewable generators. Given the expected level of constraints and curtailments in future years, a last-on-first-off de-loading policy would significantly undermine Gate 3 and the financing of its projects.

6. Deemed Firm Access

BG Energy continues to support the provision of 'deemed' firm access from a generators expected firm date. Recent changes to reinforcement plans by the SOs have delayed firm access dates of connecting assets, the cost of which is borne by the connecting party even though grid development is out of their control. This is an unacceptable reality, particularly as there are no obligations or incentives on the SOs to fulfil the provisions of a connection agreement.

The RAs view that there continues to be no convincing case for the introduction of deemed firm access has not been qualified by any depth of analysis. Recognising that new investors should not be incentivised to build ahead of the grid, it is hard to reconcile how the stated renewable targets on the island can be met unless some form of incentive is also placed on the SO to deliver the grid in a timely manner. To this end, BG Energy has suggested the development of a 'contractual framework' for the

connection of assets, which will essentially levy the cost and risk of managing developments on the respective parties and will provide certainty to investors around their project delivery and finance. Deemed firm access should at the very least be put in place for Gate 1 & 2 projects.

7. Determination of SMP when Demand is met by Price Takers, Treatment of Variable Price Takers and Quantity of Generation Paid at PFloor.

The RAs proposal that the market PFloor remains as a lower limit to the SMP and that it is consulted upon annually seems largely reasonable. However, there is an anomaly under certain circumstances, namely at night, when prices are negative despite the fact that conventional generation can be running at minimum stable generation. The current rules do not allow conventional plant running at minimum stable generation to set the SMP. This should be amended to reflect the true cost of generation at these times.

Finally, the RAs proposals to change the market rules such that; a) Variable Price Takers that are non-firm are no longer treated as firm and b) to cap the number of generators charged PFloor in an excessive generation event at total system demand are both reasonable proposals and the market rules should be changed accordingly.

Summary and Conclusions

The RAs proposals with respect to the treatment of firm access and construction of the market schedule would represent significant changes to the founding principles of the SEM and would create huge uncertainty and risk for existing and new investors to the market. Furthermore, the proposal to implement these changes once a ‘material level of harm threshold’ has been reached (but as yet undefined) would not alone create open-ended uncertainty in the market, but would strand existing generation assets and make the development and investment in new generation un-financeable.

A number of steps can be taken within the current market design to minimise the effect of increasing levels of intermittent generation on constraint costs without compromising the fundamentals of the SEM. These include:

- Reducing the mismatch in grid and generation assets by using a ‘deemed firm access’ or a ‘contractual framework’ approach to incentivise the timely investment by both the SOs and connecting generation assets;
- Developing a robust ancillary services market such that those parties providing reserve and other services which facilitate and support the system are adequately incentivised and rewarded;
- Appropriately incentivising and penalising respective parties for compliance and non-compliance respectively with grid code provisions, and
- Providing greater transparency around the derivation of the dispatch schedule so that parties can understand and anticipate changes in the dispatch schedule.

In levying costs on the affecting parties and not on customers or other market participants, these changes will provide for a more cost reflective and effective market, without the need for changes to the fundamental design or principles of the SEM.

I hope you find the comments and proposals above helpful in your review. I would welcome an opportunity to discuss them with you in more detail at a suitable time, but in the meantime, please do not hesitate in contacting me if you have any comments or queries.

Yours sincerely,

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Bord Gáis Energy