

Single Electricity Market

DS3

System Services Second Consultation

SEM Committee Cover Note

12 June 2012

SEM-12-035

Introduction

The TSOs have been engaged in the DS3 programme for a number of months. A number of documents, work-plans, consultation papers and grid code modifications have been published at this stage. The SEM Committee and the Regulatory Authorities (RAs) have been working with the TSOs both prior to and since the commencement of the DS3 programme.

Delivering a Secure Sustainable Power System (DS3)

The SEM Committee's principal objective in relation to the Single Electricity Market is to protect the interests of consumers of electricity on the island of Ireland. The SEM Committee does this by promoting competition in the SEM and by ensuring that the SEM structures are designed with the welfare of consumers at their core. In addition, when carrying out its functions in the manner most appropriate to deliver its principal objective, the SEM Committee must have regard to security of supply, sustainability and the promotion of the use of energy from renewable sources.

Considering these objectives and bearing in mind the results of the Transmission System Operators (TSO's) suite of Facilitation of Renewables Studies (FORS) published in June 2011¹, the SEM Committee in Q3 2011 requested that the TSOs put together a programme of actions and initiatives necessary to address the system operation challenges identified in the FORS.

This resulted in the development of the TSO's DS3 programme – *Delivering a Secure, Sustainable Power System* – details of which were published on the TSO's websites in December 2011. In endorsing the TSO's DS3 programme, the SEM Committee has requested that the TSOs bring a suite a recommendations and grid code modifications to the SEM Committee, or to the individual RA where appropriate, where regulatory changes were required to deliver the objectives of DS3.

The DS3 programme is a TSO led series of work-plans and initiatives, requiring significant industry and regulatory input and oversight. If fully implemented the DS3 programme will deliver significant changes to the operation of the SEM on the island, not least the facilitation of instantaneous penetration of renewable electricity of up to 75% and associated reduction in curtailment levels.

Given its statutory functions, the SEM Committee has an important role in the DS3 programme. The SEM Committee's key objective is to ensure that the interests of the all-island customer are protected throughout the DS3 project. It will do this by:

- Oversight of TSOs activities and project monitoring throughout;
- Review the impact and appropriateness of the various options and proposals put forward by the TSOs;
- Making key decisions on TSO proposals/ recommendations which will only be implemented after consultation with industry stakeholders. This is particularly evident on key workstreams such as the System Services review; and
- Ensuring consistency across SEM activities and that that the full implication of all actions proposed by the TSOs is considered.

¹Please refer to the paper [here](#)

The SEM Committee is also mindful of the interaction with other European Integration workstreams, including the implementation the EU Target Model, European Member State energy policy objectives and their implications on the DS3 programme. The aim is to reach the target model in a manner which provides benefits for consumers and is cost effective. Key drivers which will impact these workstreams include increased interconnection, moves toward regional integration of electricity markets across Europe and increased intermittent generation. With regard to intermittent generation the review of System Services is one of the key workstreams in the DS3 programme.

System Services Review

The SEM Committee has outlined its view to the TSOs that clarity around system services structures, products and remuneration in a timely manner are important. This will help to ensure that appropriate incentives are in place to facilitate investment decisions that deliver a secure supply to customers at competitive and reasonable prices. The TSO's scope of work for the System Services workstream and the associated timeline has been published by the TSOs website.²

The System Services review is intended to ensure adequate system services (also referred to as Ancillary services) are available to meet the needs of the electricity system over the coming years, in particular as a result of system operation challenges resulting from delivery of the 2020 renewables policy objectives on the island. The TSOs have a statutory duty to procure the necessary and appropriate system services in order to operate the system in a secure and reliable manner. However, this must be done in an efficient and cost effective manner. For this reason the RAs and the SEM Committee are responsible for ensuring that efficient levels of system services are recovered through electricity tariffs.

As noted in the TSOs consultation paper (*System Services second consultation*)³ the objectives of the review outlined by the TSOs are: to clarify system needs – now and projected for the future; to review the effectiveness of existing services and payment structures; to develop new services; to determine appropriate valuations of these services and to develop new/revised payment structures that foster a continued focus on performance and where appropriate drive investment and to develop an appropriate timetable for the implementation of any new arrangements in order to provide early signals to investors.

The TSO's first consultation of this process was published on 13 December 2011⁴ and sought views from the industry on the scope of the review, the structures for System Services, eligibility considerations, the contractual arrangements and the degree of interaction with the wholesale market. Following this consultation, the TSOs, with the RAs in attendance, met with interested parties on a bilateral basis.

TSO Consultation (*System Services second consultation*)

The RAs and the SEM Committee recognise that the review is still effectively in an early stage and the contents of *System Services second consultation* reflect that. However, the RAs and SEM Committee also recognise that this is an important review in the context of the 2020 renewables target on the island and the potential impact that the outcome of this review may have on the costs faced by the all-island customer.

² Please refer to the DS3 Programme Overview document on [this](#) webpage.

³ Please refer to the paper [here](#).

⁴ Please refer to the paper [here](#).

Stakeholders should be aware that, throughout this process, the SEM Committee will remain fully cognisant of its primary duty accorded under Section 9 of the SEM Act and the SEM Order⁵ – that of the protection of the interests of consumers of electricity in Northern Ireland and Ireland.

The SEM Committee has considered the TSO's consultation paper (*System Services second consultation*) and has decided that the paper should be published now for consultation in order to gain the views of the industry on the requirement for system services, outlined by the TSOs and the products proposed by the TSOs. The SEM Committee notes however that this paper (*System Services second consultation*) does not outline the proposed value of the system services, the levels of remuneration proposed by the TSOs for System Services or the proposed cost to the all-island customer.

Therefore, while sanctioning the publication of this consultation; it is the view of the SEM Committee that the paper should be considered as the next step in the broader consultation on system services products. The SEM Committee will not approve the proposed products until the full review is completed, including full industry consultation on system services values, costs to consumers, benefits to the system and consumers and remuneration to service providers.

Responses to the paper *System Services second consultation* will be reviewed and carefully considered by both the TSOs and RAs. These comments and any responses to future consultations or proposed decisions will be considered by the SEM Committee before formulating any final decision on the proposals put forward in the System Service review. Although not expressly detailed in the paper *System Services second consultation*, the RAs at this point consider that the following issues will need to be addressed over the course of the review, before any final SEM Committee decision can be made. These issues have been discussed with the TSOs and will be built into future consultation papers on this topic.

SEMC views on key issues to be covered in System Services Review

1. Types and levels of services required

The final proposal(s) for consideration by the SEM Committee will need to outline the types of services, structure of services and level of services required. The proposal(s) should be justified on the basis of robust modelling, as well as drawing on SEM and international experience. The RAs believe it important to avoid a situation where required system services are over/under incentivised based on anticipated system needs. The value of system services to the electricity system will also need to be outlined.

Furthermore, there should be a link between the levels required and the effect on the System Services revenue requirement, e.g. a requirement for an extra X amount of Primary Operating Reserve is anticipated to result in an X% increase in the System Services revenue requirement.

⁵ Please refer to the Electricity Regulation (Amendment) (Single Electricity Market) Act 2007 which can be found [here](#) and the Electricity (Single Wholesale Market) (Northern Ireland) Order 2007 which can be found [here](#).

2. Effect on the System Services requirement

The estimated effect on the revenue requirement of the System Services requirement will need to be outlined. Essentially, how much will the System Services requirement need to change by in order to incentivise the connection of sufficient flexible plant, which can provide the system services, needed for the secure operation of the power system?

3. Effect on the Capacity Payments Mechanism (CPM)

Like the effect on the System Services requirement the SEM Committee will need to be advised of the estimated effect on the CPM, such as the effect on the revenue earned by the Best New Entrant (BNE) plant. For example, if the new services offered are obtainable by the BNE plant then this would be considered as additional revenue earned by the BNE peaker. This additional revenue earned will be reduced from the BNE Peaker Cost (€/kW/yr), the net result of which is to reduce the CPM when this element is multiplied out with the capacity requirement. Alternatively, if the BNE does not offer these services (not earn additional revenue) then this will not be reduced from the CPM.

This consideration should be carried out with regard to the total revenue available in the SEM. Ultimately if the SEM Committee is provided with a proposal for increases in system services, the RAs consider at this point that there will need to be re-balancing or contribution (in some form) from the other revenue streams in the SEM paid for by the all-island customer.

4. Net benefit to the all-island consumer

The estimated net benefit to the all-island consumer resulting from the combination of the proposals will need to be detailed to the SEM Committee. It is considered that reaching the 2020 renewables target and the reduction in curtailment levels will have a dampening effect on the System Marginal Price and carbon production, which is of benefit to the all-island consumer. The potential for lower Dispatch Balancing Costs and reduced economic loss (lower curtailment) should also be considered in any final proposal(s) to the SEM Committee. While this is not an exhaustive list, it will be important that the 'business case' for new system services and their cost is fully outlined.

5. Performance monitoring

The treatment of Generators who do not provide services, when required by the TSOs and who have offered those services will need to be detailed. Whether the current Generator Performance Incentives provide the proper incentive for Generators to maintain their capability to provide services or whether further steps are required, will need to be detailed to the SEM Committee.

6. The procurement of System services

How the TSOs will propose to procure system services, i.e. through bilateral contracts, open tendering, auctions, a mix of format etc, will need to be detailed further to the SEM Committee. The format of any potential contracts should also be provided, such as the need for short versus long-term contracts in providers. The additional question of whether windfarms can provide system services (including levels and types of

services and scenarios where these services can be provided) will need to be addressed.

This list is non-exhaustive and any further important matters which arise of out consultation with industry will be examined prior to any final SEM Commission decision on the DS3 System Services review.

Next steps

- The closing date for responses to the consultation paper (*System Services second consultation*) is Friday 3 August 2012.
- After the review of responses to the *System Services second consultation* by both the TSOs and RAs a further consultation (or proposed decision paper) will be published in early Q3 2012.
- A final SEM Committee decision on the new System Services structures, products and remuneration is expected by Q4 2012.