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Date: 18<sup>th</sup> of November 2016

RE: Offers in the I-SEM Balancing Market Consultation Paper(SEM-16-059)

Dear Brian and James,

EAI welcomes the opportunity to respond to this consultation. However, we believe that the overly prescriptive proposals outlined therein will systematically deny legitimate cost recovery in the I-SEM market. This is clearly not in the best interests of consumers as it would distort competition and threaten security of supply, by generating inappropriate exit signals in the short term and deterring future investment given the heightened perception of regulatory risk that would persist<sup>1</sup>. We would therefore welcome an opportunity to engage directly on these important issues before any decision is taken.

### **Specific Concerns**

Specifically, we are concerned that the consultation paper does not set out a principles-based approach similar to the current BCoP<sup>2</sup> and that the prescriptive options presented would result in generators being unable to recover legitimate cost items including some significant elements of variable maintenance costs, foregone revenues, and reasonable provision for increased risks. The SEMC's proposed dismissal of these cost items is without any valid justification and is all the more unexpected given that the SEMC previously considered such costs explicitly in a 2008 Inquiry and decided that they should be included in generators' SRMC<sup>3</sup>.

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<sup>1</sup> Increased regulatory risk will undermine conditions for investment.

<sup>2</sup> Both of the options presented in the consultation paper are based upon a prescriptive approach that attempts to define the eligibility of cost items. This is impractical and will lead to substantial issues relating to errors, incompleteness and management of future changes that will have a substantial negative impact on the market.

<sup>3</sup> SEM Committee (2008), Complaints on Bidding Practices in the Single Electricity Market: SEM Committee Inquiry, Final Report, SEM-08-069, 12 June 2008, pages 31-32.

In addition, EAI does not support the proposal to reference any bidding controls in a subsidiary document to the license and believes a principles-based approach which affords, at least, the current level of recourse to legal review/appeal provides a necessary accountability mechanism by which the long-term interests of consumers are protected. The proposed changes in the consultation paper have the effect of diluting the current level of recourse for participants to legal appeal/review.

We furthermore note that insufficient evidence has been offered to support a move away from the current approach<sup>4</sup>. The efficacy of the current principles based approach is recognised and its success acknowledged.

*“... the SEM Committee’s view is that the current BCoP has been effectively enforced through monitoring and investigations, and it has likely prevented market power abuses...” P.10*

There is furthermore no justification whatsoever for a *reversal* of the SEM Committee’s position in 2008, which was based on sound economics, that *“Operation within the market must be economically viable for competition to flourish. The SEM Committee considers that this can only be achieved by ensuring that all avoidable costs are recoverable”*<sup>5</sup> – such costs, the SEM Committee concluded then, should include *“the additional O&M expenditure, the additional equipment costs, the increased risk of failure to plant and equipment as a result of the plant’s running regime and the concomitant loss of revenue from capacity payments and infra-marginal rents from SMP”*<sup>6</sup>.

Our wider concerns regarding the proposals set out in the consultation paper are detailed below.

### **Unintended Consequences**

- The SEM Committee proposals go beyond what is necessary and will have serious adverse negative implications for the entire market.
  - In conjunction with emerging CRM parameters, the proposals appear to amount to over-regulation and capping of energy and capacity prices. This reinforces the impression that I-SEM will be a heavily regulated (below)cost-based market.
  - The proposals significantly increase the risk of under-recovery of costs (missing money), inefficient market exit, and distorting investment signals in the market into the future.

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<sup>4</sup> The ability to challenge decisions should be viewed as strength of the current process and not as a weakness. Given the complexities of the matters at hand and the consequences for participants of the regulators getting decisions wrong, having an appropriate appeals mechanism would seem prudent and in the best long term interests of consumers.

<sup>5</sup> Ibid footnote 3, para 9.9.

<sup>6</sup> Ibid footnote3, para 9.8.

### Proposed License Changes

- The SEM Committee proposals to move generators rights and obligations with regards to bidding to a subsidiary document is unacceptable. If there is to be a condition placing restrictions on how a generator bids, it must be in the licence as opposed to a subsidiary document.
- Insufficient explanation and justification has been provided in the Consultation Paper on the proposals being brought forward and on the changes being made to cost valuation compared to today's approach.
- The SEM Committee must bring forward well explained and justified rationale for any impositions it seeks to place on generators.

### Conclusion

- In this response, EAI has outlined a number of major concerns regarding the proposals put forward by the SEM Committee.
- No valid justification or evidence has been offered to explain the significant move away from the existing bidding control framework which has proven successful and better fulfils the SEMC's assessment criteria than the options put forward in the consultation paper.
- There is furthermore no justification whatsoever for a *reversal* of the SEM Committee's decision in 2008 on allowable cost items, which was based on sound economics.
- We would therefore welcome further engagement with the SEM Committee and a meeting or workshop to establish a common understanding of the potential implications on the market.

Yours sincerely,



Stephen Douglas  
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Electricity Association of Ireland (EAI)