



IWEA response to the European Commission consultation on Generation adequacy, capacity mechanisms and the internal market in electricity

07 February 2013

Introduction

The Irish Wind Energy Association (IWEA) welcomes this opportunity to respond to the European Commission consultation on Generation Adequacy, Capacity Mechanisms & the Internal Market in Electricity. IWEA is Ireland's leading renewable energy representative body representing more than 200 members involved in wind and renewable energy development in Ireland and Northern Ireland (through the Northern Ireland Renewables Industry Group (NIRIG), set up in collaboration with Renewable UK). IWEA represents members with projects across the spectrum, in operation, under construction and awaiting connection. In Ireland IWEA members are involved in the majority of connected projects but also involved in more than 85% of the MW of currently grid contracted projects.

Through NIRIG we represent more than 25 company members that have developed over 85% of renewable generation operational in Northern Ireland today and who will contribute a significant majority of renewable energy required to deliver the 2020 targets.

The IWEA membership base includes all large, medium and many small developers as well as financial, legal advisory, consultancy, contractors and other service providers involved in the renewables sector in Ireland and Northern Ireland.

Comments on Consultation

IWEA believes that the completion of the Internal Energy Market will bring significant benefits for European citizens of more choice, cheaper prices, better service and improved security of supply. However, we believe that the policy and regulatory developments supporting the IEM still face significant obstacles.

At present, some electricity markets do not deliver adequate long-term investment signals to provide the confidence needed to invest in electricity generation, and capacity mechanisms are used to ensure investment takes place. Other markets, such as Single Electricity Market (SEM) on the island of Ireland, have integrated capacity payment mechanisms which are an integral part of market design.

- Providing a stable and predictable regulatory framework could contribute to increasing investment in new capacity. Any changes to existing capacity mechanisms need to ensure that market risk is not being replaced by regulatory risk.
- IWEA considers that Member States are best placed to consider whether there are capacity adequacy concerns in their state and to introduce measures (such as capacity payment

mechanisms) to combat such problems. It must be borne in mind that different states face different issues depending on geographic location, interconnection, generation portfolio mix and age, levels of indigenous fuels etc.

- We consider that CPMs can be designed so as to be compatible with cross-border trade. We would agree that once the Target Model has been implemented and we have a better understanding of how well markets and trades are operating, then there could be an opportunity to revisit the methodologies of assessing generation adequacy and capacity payment mechanisms.
- Capacity mechanisms are an essential part of the SEM in Ireland; the rationale is that energy payments are designed to recover variable costs (generators must bid at short run marginal cost) and capacity payments recover a portion of fixed costs; with the aim of meeting the long run marginal cost of generation.
- As an island system with limited interconnection it is essential that Ireland has the ability to manage its own generation adequacy and to incentivise generation when it is required. The SEM capacity mechanism operates such that the capacity payment per MW is higher when there is less capacity available. While interconnection can provide some benefits in terms of the provision of reserve, the reality is that interconnection capacity is limited and has had proven reliability issues. In recent times there have been a number of outages of the Moyle Interconnector linking Northern Ireland to Scotland. This serves to emphasise that the reliance on cross border activity for generation adequacy is not necessarily appropriate in all cases.
- On the island of Ireland, the SEM currently has a capacity mechanism which has been effective in ensuring that the market is attractive to developers of electricity generation. There are still some concerns regarding generation adequacy in Northern Ireland, however the limiting factor is currently infrastructure build-out, in particular the North South Tie Line.
- The capacity payment mechanism in the SEM is market related and based on sound economic principles. It has a proven track record, is independently assessed, transparent, non-discriminatory and technology neutral. These should form the basis of any market related mechanism.
- It is essential that any capacity mechanism has a clearly defined objective relating to the provision of generation adequacy. Plant flexibility is a different characteristic albeit equally vital to support the integration of large amounts of renewables to meet Europe's renewable energy targets. Flexibility should be appropriately incentivised through ancillary services and generation adequacy should be addressed through capacity mechanisms. As a general rule the two mechanisms should not overlap, the distinction being that capacity mechanisms are technology neutral and should ensure there is sufficient generation in megawatts to meet demand – i.e. ensure generation adequacy. A well functioning ancillary services regime should help deliver the right type of generation mix by rewarding flexibility.
- In order to facilitate the renewable targets which have been set for 2020 it is important to have support for renewable energy to enable it to get into the market and gain sufficient market

share. RES support as well as priority grid access and dispatch are not a market distortion undermining investment in other technologies, but they are a support for new entrants given the structural risks faced by a technology which has not yet reached market maturity and in order to facilitate achievement of the EU's 2020 RES-E targets. RES supports were introduced to incentivise investment in the short term such that it would bring long term benefits to Europe's competitiveness and sustainability as well as independence from imported fossil fuels. To the extent that they did not exist, Europe would not meet its renewable targets and a trade-off must be realised. Notwithstanding that – renewable supports will have to be phased out in time once RES costs come in line with thermal generation and markets are more appropriately structured to provide a return on investments. Capacity mechanisms may still be needed after that though as reduced SRMC prices may still not give the appropriate signals for capacity in localised areas.

Consultation Questions

(1) Do you consider that the current market prices prevent investments in needed generation capacity?

The SEM has integrated capacity payment mechanisms which are an integral part of market design. Capacity mechanisms are an essential part of the SEM; the rationale is that energy payments are designed to recover variable costs (generators must bid at short run marginal cost) and capacity payments recover a portion of fixed costs; with the aim of meeting the long run marginal cost of generation. Providing a stable and predictable regulatory framework could contribute to increasing investment in new capacity.

(2) Do you consider that support (e.g. direct financial support, priority dispatch or special network fees) for specific energy sources (renewables, coal, nuclear) undermines investments needed to ensure generation adequacy? If yes, how and to what extent?

In order to facilitate the renewable targets which have been set for 2020 it is important to have support for renewable energy to enable it to get into the market and gain sufficient market share. RES support as well as priority grid access and dispatch are not a market distortion undermining investment in other technologies, but they are a support for new entrants given the structural risks faced by a technology which has not yet reached market maturity and in order to facilitate achievement of the EU's 2020 RES-E targets. RES supports were introduced to incentivise investment in the short term such that it would bring long term benefits to Europe's competitiveness and sustainability as well as independence from imported fossil fuels. To the extent that they did not exist, Europe would not meet its renewable targets and a trade-off must be realised.

- (3) Do you consider that work on the establishment of cross-border day ahead, intraday and balancing markets will contribute to ensuring security of supply? Within what timeframe do you see this happening?**

IWEA believes that the completion of the Internal Energy Market will bring significant benefits for European citizens of more choice, cheaper prices, better service and improved security of supply. However, we believe that the policy and regulatory developments supporting the IEM still face significant obstacles.

- (4) What additional steps, if any, should be taken at European level to ensure that internal market rules fully contribute to ensuring generation adequacy and security of supply?**
- (5) What additional steps could Member States take to support the effectiveness of the internal market in delivering generation adequacy?**
- (6) How should public authorities reflect the preferences of consumers in relation to security of supply? How can they reflect preferences for lower standards on the part of some consumers?**
- (7) Do you consider that there is a need for review of how generation adequacy assessments are carried out in the internal market? In particular, is there a need for more in depth generation adequacy reviews at:**
- a. National level**
 - b. Regional Level**
 - c. European Level**

IWEA considers that Member States are best placed to consider whether there are capacity adequacy concerns in their state and to introduce measures (such as capacity payment mechanisms) to combat such problems. It must be borne in mind that different states face different issues depending on geographic location, interconnection, generation portfolio mix and age, levels of indigenous fuels etc.

We consider that CPMs can be designed so as to be compatible with cross-border trade. We would agree that once the Target Model has been implemented and we have a better understanding of how well markets and trades are operating, then there could be an opportunity to revisit the methodologies of assessing generation adequacy and capacity payment mechanisms.

- (8) Looking forward, is the generation adequacy outlook produced by ENTSO-E sufficiently detailed? In particular,**
- a. Is there a need for a regional or European assessment of the availability of flexible capacity?**
 - b. Are there other areas where this generation adequacy assessment should be made more detailed?**
- (9) Do you consider the Electricity Security of Supply Directive to be adequate? If it should be revised, on which points?**

(10) **Would you support the introduction of mandatory risk assessments or generation adequacy plans at national and regional level similar to those required under the Gas Security of Supply Regulation?**

(11) **Should generation adequacy standards be harmonised across the EU? What should be that standard or how could it be developed taking into account potentially diverging preference regarding security of supply?**

See Question 7 above

(12) **Do you consider that capacity mechanisms should be introduced only if and when steps to improve market functioning are clearly insufficient?**

This would depend on the market structure in a particular region. See Question 1 above

(13) **Under what circumstances would you consider market functioning to be insufficient:**

a. to ensure that new *flexible* resources are delivered?

b. to ensure *sufficient* capacity is available to meet demand on the system at times of highest system stress?

It is essential that any capacity mechanism has a clearly defined objective relating to the provision of generation adequacy. Plant flexibility is a different characteristic albeit equally vital to support the integration of large amounts of renewables to meet Europe's renewable energy targets. Flexibility should be appropriately incentivised through ancillary services and generation adequacy should be addressed through capacity mechanisms. As a general rule the two mechanisms should not overlap, the distinction being that capacity mechanisms are technology neutral and should ensure there is sufficient generation in megawatts to meet demand – i.e. ensure generation adequacy. A well functioning ancillary services regime should help deliver the right type of generation mix by rewarding flexibility.

(14) **In relation to strategic reserves:**

a. Do you consider that the introduction of a strategic reserve can support the transition from a fossil fuel based electricity system or during a nuclear phase out?

b. What risks, if any, to effective competition and the functioning of the internal market do you consider being associated with the introduction of strategic reserves?

(15) **In relation to capacity markets and/or payments:**

a. Which models of capacity market and /or payments do you consider to be most and least distortionary and most compatible with the effective competition and the functioning of the internal market, and why?

b. Which models of capacity market and /or payments do you consider to be most compatible with ensuring flexibility in a low carbon electricity system?

c. Are there any models of capacity mechanism the introduction of which would be irreversible, or reversible only with great difficulty?

We would agree that once the Target Model has been implemented and we have a better understanding of how well markets and trades are operating, then there could be an opportunity to revisit the methodologies of assessing generation adequacy and capacity payment mechanisms.

(16) Which models of capacity mechanisms do you consider to have the least impact on costs for final consumers?

(17) To what extent do you consider capacity mechanisms could build on balancing market regimes to encourage flexibility in all its forms?

(18) Should the Commission set out to provide the blueprint for an EU-wide capacity mechanism?

See Question 7 above

(19) Do you consider that the European Commission should develop detailed criteria to assess the compatibility of capacity mechanisms with the internal energy market?

See Question 7 above

(20) Do you consider the detailed criteria set out above to be appropriate?

a. Should any criteria be added to this list?

b. Which, if any, criteria should be given most weight?