

IWEA response to the Consultation on I-SEM Market Power Mitigation

18 January 2016

IWEA welcomes the opportunity to respond to the consultation paper on Market Power Mitigation in the I-SEM.

The area of Market Power is something that needs to be addressed in such a small market with limited competition. The increased trade with other markets which is anticipated with the new market design also opens the potential for market power abuse from other markets. Any analysis carried out under this workstream should look not only at the current market participants, but also the likely changes which will take place during the lifetime of the market. This all needs to be given due consideration in terms of market power mitigation measures.

There are a number of areas where we consider that market power could have a significant impact for wind generation:

- The availability of PPAs through a range of suppliers is also of particular importance to the wind industry. The provision of an Aggregator of Last Resort is an important aspect in ensuring there is a route to market for all generators. IWEA welcomes that this will be an enduring feature of the market.
- There needs to be clear provision for asset-less traders in the market which will increase liquidity in a number of market timeframes. This will help reduce the impact of any potential market power by increasing the number of participants and the level of competition.
- The discussion mentioned measures such as a Bidding Code of Practice (BCOP). BCOP has been a successful measure to control bidding behaviour in the current SEM and is worth consideration in some form, especially for the balancing market, in light of the need for transparent balancing prices and a suitable transition to balance responsibility for wind generators. However it is essential that any measure which is introduced does not put participants in I-SEM at a disadvantage relative to market participants in other jurisdictions or lead to market distortion. Taking these different requirements into account, IWEA believes that a form of Bidding Code of Practice would be appropriate for the Balancing Market in particular. Consideration should be given to principle based market power mitigation in the other market timeframes.
- Day Ahead Market: Since the algorithm EUPHEMIA is the exclusive route to market for participants in the Day Ahead Market in I-SEM, Market Power here is not considered to be as important a factor as in some of the other timeframes. This market is also unconstrained so there is no opportunity to exercise locational market power. However, the consultation paper notes that there is likely to be Market Power concerns in all timeframes, therefore a principles based market power mitigation measures is needed for the DAM and IDM.

- **Intraday market:** It is essential that there are measures in place to ensure a liquid intraday market so that wind participants can update their trades based on improved forecasting. In our response to the I-SEM Markets consultation IWEA welcomed the proposal to introduce intra-day auctions, and we proposed that these should be introduced on an enduring basis rather than just as a transitional measure. These will allow greater liquidity at certain timeframes and will enable increased intraday trading to take place. It is essential that this is coordinated with GB to ensure there is increased liquidity. The largest concerns for wind are both in terms of price (intraday and balancing) and liquidity (intraday). IDM auctions do help with price and liquidity. Market-making measures such as mandating some volumes of trade intraday could be considered for participants which are thought to be in a position to exercise market power. IWEA is concerned at the lack of clarity in relation to the operation of the Intra-Day Market at this time due to the potential costs that the introduction of balance responsibility brings for wind generators and the concern around the availability of tools such as a liquid intraday market to mitigate that balancing risk. As above, a principle based approach should be considered.
- **Balancing Market:** The introduction of prescriptive bidding through a Bidding Code of Practice in the Balancing Timeframe would mitigate any potential locational market power abuse as it is in this timeframe that the constraints are taken into account. In particular wind generation in the I-SEM is more likely to be exposed to imbalance pricing arising from errors in wind forecasting. Wind generators should not be exposed to the costs of meeting network constraints as the imbalance price should only take into account energy balancing actions. However, there is still a need to address constraint bidding in the balancing market to protect consumers from additional costs through higher DBC charges. Actions which promote cost reflective energy pricing rather than distortions which result in higher pricing would be welcomed. A BCOP in this timeframe would ensure that market participants who might otherwise be in a position to exercise market power (whether size or location related) would be prevented from doing so. This would be particularly relevant at times of scarcity. Further consideration may be required in relation to the BCOP to be used, e.g. whether it is based on the short run marginal cost, or what criteria can be taken into account.
- **Forwards:** Consideration could be given to the promotion of balancing contracts in forward contracts which will provide a hedge for wind generation which may be exposed to imbalance pricing.
- There may be potential for market power interactions between Energy Markets, Capacity and DS3 given that all will require bidding through auctions by market participants, and this will need to be addressed.

IWEA response to Consultation Questions:

Do you agree with the policy developments and trends identified as potentially impacting on an I-SEM market power mitigation strategy?

IWEA agrees with the policy developments and trends identified.

Are there other factors not identified here which you consider relevant?

It is important in all these discussions and considerations to keep in mind national policy objectives of moving to a decarbonised energy system. The recent DCENR publication “Ireland’s Transition to a Low Carbon Energy Future” sets out a vision for transforming Ireland’s fossil fuel-based energy sector into a clean, low carbon system by 2050. The paper states:

“Our vision of a low carbon energy system means that greenhouse gas (GHG) emissions from the energy sector will be reduced by between 80% and 95%, compared to 1990 levels, by 2050, and will fall to zero or below by 2100.”

It is also important to bear in mind that the ISEM market redesign represents a radical change for market participants, not least wind generators who will now face balance responsibility for the first time. As wind generators become more market-facing there is a need for the tools to be in place to enable wind generators to mitigate this balancing risk without undue additional costs. This impacts on the Market Power work stream as it has been shown in the consultation that market power will remain an issue in the balancing market in particular.

Do you agree with the proposed appropriate markets/trading periods for assessing market power in I-SEM’s energy and financial markets?

IWEA agrees that an assessment should be made in relation to the markets/trading period identified in the consultation paper. While an assessment is worthwhile in each timeframe, the needs may vary as outlined in our introduction.

Do you agree with the proposed geographic scope of the proposed markets/trading periods?

As outlined in the paper the geographic scope will vary depending on the timeframe which is being assessed (e.g. the day ahead market is unconstrained therefore the island of Ireland needs to be considered, whereas as locational concerns would need to be taken into account in the Balancing timeframe).

Do you agree with the proposed definition of competitive behaviour and pricing in I-SEM?

The opportunity cost may not align with the SRMC. In the case of supported renewable generation that is constrained or curtailed, the opportunity cost is the lost revenue from the support scheme which is only paid for electricity generated.

Do you think that the suggested examples in which market power can be exercised in I-SEM captures the relevant issues?

The examples provided appear to capture the relevant issues. In particular IWEA has concerns in relation to the lack of liquidity in the intraday market through potential withholding of capacity, and artificially high prices in the balancing timeframe.

Do you agree that the potential for market power abuse in I-SEM appears to be weaker in the forward financial market compared to the physical markets?

N/A

Do you agree with the implications for market power arising from interactions between the physical markets, CRM, FTRs and DS3 System Services as shown above?

The interactions between these markets are important. In relation to the DS3 system services, the decision from the SEM Committee is that, where there is not sufficient competition, an auction will not be run and regulated tariffs would be used. This has been introduced in an effort to mitigate market power concerns. IWEA would note that, while there is a need to ensure that there is no abuse of market power, the required system services need to be delivered and the incentives need to be in place to ensure delivery of these services.

Do you agree that these are the appropriate metrics to identify market power ex-ante and ex-post in I-SEM?

IWEA agrees that the appropriate metrics have been identified. It is important to note that, given the two contrasting results from the two modelling methodologies (HHI is showing reducing market concentration and the RSI results indicate that there is increasing market power concerns), the modelling methodology is extremely important. Given the potential implications of market power on the different market timeframes it is extremely important that RSI is not discounted at this time.

Are there other metrics that you consider should be applied?

N/A

Do you agree with the approach taken by the RAs to modelling market power in I-SEM?

In relation to the modelling approach being used by the RAs, IWEA notes that this is consistent with other modelling methodologies. However we would urge that a scenario be identified which has increasing levels of demand (associated with new data centres connecting to the grid) and an increased contribution from renewable electricity to contribute to the expected shortfall of renewables in relation to heating and transport.

Do you agree with the conclusions for I-SEM market power that have been drawn from the modelling results?

N/A

Do you agree with the SEM Committee's view on the effectiveness of each of the SEM market power mitigation measures?

The SEM Committee's view appears to be appropriate in relation to the effectiveness of the SEM market power mitigation measures.

Are there any particular aspects of the SEM market power mitigation strategy that you think should be applied differently, especially in relation to I-SEM?

Further consideration needs to be given in relation to the BCOP. The BCOP has delivered cost reflective, transparent pricing in the SEM which has helped to attract the investment in wind generation needed to meet renewables energy targets. As outlined above IWEA believes that this may be most appropriate in the Balancing timeframe, however consideration needs to be given in relation to the opportunity cost and the type of products that can be bid into the market. This ties in closely with the detailed design on the Energy Trading Arrangements.

Do you agree with the five key principles for assessing market power mitigation policies as outlined in this section 8.3? If you think there should be alternatives, please state the reasoning.

In general, IWEA agrees with the five key principles outlined in the paper.

For the Forward Contracting Obligation: - What should be the measure and threshold that results in a market participant being included or excluded in the FCO, i.e. what is its applicability? - What should be the volume and product definition of forward contracting required from a market participant who falls under the FCO? - How should the price be set for the volume contracted under the FCO? - What type of access should buyers have to FCO volumes?

N/A

Which of the balancing market mitigation options do you consider most appropriate, i.e. MMU-triggered intervention, automated intervention via a PST or via the "flagging and tagging" approach, or prescriptive bidding controls? Where feasible please relate the preferred approach to the five key principles for this workstream of effective, targeted, flexible, practical and transparent.

The IWEA preference would be for an approach similar to the application of BCOP in the current market which is a flexible set of bidding principles. All of the options proposed for the BM are highly prescriptive and less flexible than the current BCOP. Errors are likely to emerge from any attempt to impose prescriptive rules on generator bidding and this could be detrimental to both competition and generator financing. It is much better to have a mechanism whereby each individual scenario can be considered by the MMU in light of all the evidence.

Which ex-ante bidding/offer market power mitigation options for the DA and ID markets do you favour – bidding principles and ex-post assessment, or ex-post assessment only? Where feasible please relate the preferred approach to the five key principles for this workstream of effective, targeted, flexible, practical and transparent.

As outlined in the introduction, the main concern of the wind industry in relation to these timeframes is liquidity in the intra-day market. For this reason different approaches are warranted for the Day Ahead and the Intraday market. The introduction of intra-day auctions will allow greater liquidity at certain timeframes and will enable increased intraday trading to take place. Measures such as mandating some volumes of trade intraday could be considered for participants which are thought to be in a position to exercise market power. IWEA is concerned at the lack of clarity in relation to the operation of the Intra-Day Market at this time.

If ex-ante bidding principles were to be adopted, how flexible should they be and how would this be facilitated/enshrined in their wording?

Under what structural conditions or in combination with other market power mitigation measures should vertical ring-fencing of the incumbents be relaxed?

IWEA believes, with all the uncertainties going forward and the potential risk of market power it is imperative that ring fencing arrangements are retained.

Under what circumstances and criteria (or metrics) should the application of ring-fencing to other market participants be considered?

The Market Monitoring Unit should continue to assess market power considerations in relation to other participants.

In summary, IWEA welcomes the option to respond to this discussion paper at this time and looks forward to engaging in more detail during the formal consultation phase, at which stage we expect there will be more clarity in relation to the energy trading arrangements.