IWEA response to the DS3 System Services Consultation on Qualification Process and Contract Design

16 December 2015

The Irish Wind Energy Association (IWEA) welcomes the opportunity to comment on the consultation on Qualification Process and Contract Design.

As outlined in previous submissions, IWEA's overriding objective with the DS3 arrangements is that they must deliver the necessary system services and any required investment for services to facilitate the achievement of the 2020 renewable targets and minimise curtailment**.** The delays that have been seen to date in increasing the System Non-Synchronous Penetration (SNSP) on the electricity system are of serious concern to the wind industry, and wind generators are likely to see increasing levels of curtailment if these system services are not introduced in a timely manner, thereby putting the 2020 renewable energy targets at risk. From 1 January 2018 renewable generators will no longer receive compensation for curtailment. Given the delay in the implementation of DS3 and the commissioning of a new North South Interconnector, IWEA strongly believes that the curtailment decision needs revisited and, at least, the implementation of the decision delayed until the new system services and North South Interconnector are delivered.

It should also be recognised that the market re-design currently underway, along with changes to the capacity remuneration mechanism, bring a lot of uncertainty for generators in relation to forecasting revenues in the coming years.

It is essential that the qualification process strikes the right balance between ensuring the projects are delivered and acting as disincentive for projects to participate by creating barriers to entry for new participants.

As outlined in our previous responses IWEA believes that wind farms can play an important role in the provision of system services, however the timelines for certainty in relation to revenues is critical. There will be significant build out of wind farms in the next two years in order to be compliant with the REFIT 2 construction deadline. If these wind farms are to invest in enhanced provision of system services it is essential that there is clarity in relation to the revenues that will be available to ensure the investment case is there. There also needs to be clarity that the REFIT calculation does not take these revenues into account as this would erode the value of the investment. For wind farms connecting to the system in the next two years, many are currently signing contracts and approaching financial close for their projects. In Northern Ireland NIE has issued a moratorium on new connection offers due to the flood of new application for projects pursuing NIRO accreditation. DS3 will be required for all the projects which will be commissioned before 31 March 2017.

If there is no certainty into the likely DS3 revenues at this time these projects may not be able to deliver the required services as the investment case cannot be made. This is particularly relevant for the provision of Dynamic Reactive Response and Fast Post Fault Active Power Recovery. Barriers to entry could result in significant delays to the delivery of DS3 investments.

At the time of drafting this response, the first decision on the detailed design of the capacity mechanism has not yet been published, and so our answers have been prepared in the absence of further detailed information. The answers to the consultation questions are outlined in the following section.

Questions from the consultation paper

Question 1: Do you agree with the proposed procurement steps or have any concerns regarding the implementation of such a process? Do you consider there is a need for fewer or more steps in the procurement process? Please provide detail to support your views.

IWEA proposes that a legal opinion be obtained on the necessity of complying with the Utilities Procurement Directive for the different procurement options: regulated tariffs and auctions.

In the process proposed the service provider is offered a contract once they are deemed eligible by the TSO. However, the key details of the contract are still unknown at this point in the process. In particular, it is not known if the service in question will be based on an auction or a tariff (which determines the length of the contract for new or refurbished projects) or what the agreed clearing price of tariff rate will be.

Existing Service providers currently comply with Grid Code obligations and Harmonised Ancillary Service contractual obligations. Many of these system services have also successfully been delivered during real time system events. Therefore existing service providers should be exempt from certain procurement steps where it has already been demonstrated that the service can be provided.

Question 2: To what extent are the proposed steps also appropriate for Capacity? Do you consider there are benefits in running this process jointly for both Capacity and DS System Services? Please provide detail to support your views.

IWEA expects that a simpler process can be used in relation to capacity as there is no detailed assessment required on the part of the TSO in relation to the provision of services. The ability to provide capacity, and the type of capacity mechanism which has been chosen, do not require such a detailed qualification process, however the pre-qualification should ensure commercial and legal viability to deliver on the contract. It is also acknowledged that information will be required in relation to the expected level of participation. Experience from GB capacity market and EMR CfD is that certain parties bid below cost price in the auction, which dampened the clearing price. This resulted in projects not being delivered. The prequalification criteria, coupled with demonstrable financial commitments, such as bid bond and subsequent performance bonds, will be an important element in ensuring credible auction results and delivery of projects.

A different level of evidence may be appropriate for new vs existing providers in qualification for both DS3 and CRM. For example, existing providers would not need to show planning permission, connection agreement etc.

Question 3: Do you agree with the above outlined principles for qualification? Please provide detail to support your views.

IWEA supports the principles for qualification, and we note that the requirements should not be too onerous at this stage. We welcome the principle that the approach should encourage participation. A facility should be provided by the TSO whereby a potential service provider can be assessed to ensure that the service meets the requirements of the TSO before the auction is run to ensure a common understanding of the requirements.

Existing evidence should be used as far as reasonably practicable. For example licence and connection agreement obligations should satisfy certain qualification criteria in order to minimise unnecessary administration.

Question 4: Do you believe that the above outlined principles for qualification should also apply for the procurement of Capacity in the I-SEM? Please provide detail to support your views.

IWEA supports that the same principles should apply for capacity, noting that the process for assessing eligibility may not need to be as complex. There may be some different requirements to take account of the fact that CRM is a financial contract whereas DS3 is about physical delivery. The implications of failure to deliver are also different for CRM and DS3.

Question 5: Do you agree with the use of a bid bond as part of qualification for DS3 System Services?

In general, IWEA supports the requirement to demonstrate financial commitment as part of the qualification process. The use of a bid bond is a potential option which could be used to demonstrate financial commitment, however some clarifications are required, such as the following:

- The bid bond is only paid once the TSO are satisfied that the provider is eligible to provide the service.
- If a potential service provider is not successful in the auction, the bond will expire.
- If an auction does not arise due to a lack of competition, the bid bond should be released. If the bid bond is required as part of qualification process then there is a risk that a provider, who is planning on obtaining a long term contract for plant refurbishment, will have a bond in place prior to a decision on the level of competition. If it is decided at this time that there is insufficient competition and tariffs are put in place then this provider will not have the certainty of a long term contract and hence will not invest, thus placing the bid bond at risk. To avoid this bid bonds should only be required if and when an auction is to take place. Alternatively, the bid bond could be released if there is no auction and if the minimal commercial requirements of the plant cannot be met.

- There needs to be clarity around the auction bidding rules in advance. The pre-qualification data should determine the level of competition and whether an auction can be run or not. If there is sufficient competition there will be little incentive to bid high, however it is important that the full costs of service provision can be included in the bid. The proposal to cap bids at the tariff which might otherwise apply may not allow for the full costs of service provision to be included.
- If there is no competition, then the regulated tariff will take effect. It will be important to ensure that people submit viable information in the pre-qualification.

In the initial years of DS3 there will be considerable uncertainty, prior to an auction, as to whether or not a bidder will be successful in an auction. This is because there is no historical market data for bidders to review and the assessment process of the TSO being untested. Some projects will have made significant financial investments (planning permission, grid connection, land rights) prior to any certainty as to whether or not their project will realise any revenue under DS3. A bid bond will increase the costs a developer will incur before a contract is potentially awarded and therefore a further cost which is at risk. A bid bond could increase the barrier to entry for potential projects and increase the concentration in the auction. As an alternative to bid bonds there could be a substantial financial commitment test which could be satisfied if, for example, developers have paid grid costs associated with new service.

Question 6: Do you have views on an appropriate level for the bid bond for DS3 System Services?

Careful consideration needs to be given to the appropriate level of the bond, such that the incentives are in place to ensure the services are provided and to remove speculative bids, but that is does not act as a disincentive to participation. A €/MW penalty would seem like the simplest and most transparent approach, however other approaches could also be considered which relate to the tariffs for the products. IWEA would urge a simple approach be followed in this regard.

It should be borne in mind that before qualifying for DS3 auctions, service providers, in many cases, will already have made significant investments in their projects with no certainty of any future revenue for these projects and this should be taken into account when setting the level of the bond.

Question 7: Do your views on the level and usage of bid bonds differ for Capacity procured in the I-SEM?

The ability to participate in the Reliability Option will depend on the perceived level of risk in being able to deliver energy at times of system stress. It is important that this level of risk can be built into the bid price in for the capacity auction. IWEA is of the view that the level of risk for wind generators in the reliability auction is high and therefore the cost of the associated risk will also be high. Participation in the capacity mechanism should not be mandatory. The timing of the bid bond is important here to ensure that a generator can ascertain whether or not they are eligible before committing to taking part in the auction through provision of a bid bond.

Question 8: Do you see benefits in having a combined bid bond, covering both DS3 System Services and I-SEM capacity?

IWEA has no objection in principle to a combined bid bond. The SEM Committee must ensure that the overall credit requirements in the I-SEM and DS3 markets are optimised. This should include netting arrangements if feasible, however it is recognised that contractually it may be difficult to implement. Existing system service providers will have a credit exposure to the TSO which could be considered and further investigated for potential netting arrangements in order to optimise the amount of credit which is required.

It is important that the bid bond is fit for purpose, therefore there would not appear to be any increased efficiency in combining the bonds in terms of covering the risks associated with non-delivery.

Question 9: Are there any approaches, in addition to those identified above, for identifying whether providers are new or existing?

The approach for "new" service providers would seem appropriate. It is less clear how the "material investment" levels will be assessed. It is essential that long term contract can be provided for material investments. It is not clear how the approaches put forward will work in practice.

Question 10: Do you have views on an appropriateness of each of the proposed approaches?

It is not clear which of the proposed approached is most appropriate. The lack of available data would make approach 1 more difficult to implement, and therefore Approach 2 may be more appropriate at first, however this approach appears to be more subjective in nature.

Question 11: Do you have a view on whether and how the above approaches could and should be applied for the procurement of Capacity in the I-SEM?

These approaches would not appear to be necessary for capacity as this is not a new service similar to system services.

Question 12: Do you have a view on the proposals relating to existing plant as outlined above? Please outline any changes you would like to see to the above processes.

IWEA supports the sentiment that the highest level of system services should be obtained from existing plant where appropriate, however it is essential that this is done in a manner that does not expose the provider to any additional commercial risk which is not provided for through payment for the services provided. In particular we would urge caution when targeting particular services. An example being Fast Post Fault Active Power Recovery, while this is available from most existing providers it will be of most benefit to the TSO when provided by existing and future renewables. In this regard, the provision of this service from existing plant should not impede its provision by future renewable plant.

There are grid code obligations to provide certain system services. This obligation ensures existing providers will continue to provide system services otherwise they will be in breach of their Generation Licence. We are concerned with mandating a level of service above the Grid Code requirement. System service providers must be provided with the discretion as to whether or not they will participate in the commercial arrangements as they may form a view that the level of remuneration is not sufficient to cover the level of risk associated with the commercial arrangements.

Question 13: Please can you outline your views on the proposed general criteria outlined in 5.1 and provide suggestions/comments on how appropriate these are for technology providers and potential System service providers.

IWEA welcomes clarity in relation to the criteria that have been outlined. However concerns arise in relation to the subjectivity of a number of these criteria, for example what constitutes and "acceptable environmental track record". Further detail would be required on what the exact requirements are. In relation to financial criteria, it is important to ensure that the criteria do not discriminate unduly against new entrants.

Question 14: Please detail your views on the options outlined for assessment of grid connection, planning consent, and environmental and other permits/licenses – what are the options you consider to be most appropriate in ensuring sufficient Systems Services are procured to enable SNSP levels to be accommodated as envisaged under the DS3 programme.

IWEA would support the proposal of the three criteria of Grid, Planning and Environmental/ Construction Permitting. The options provided for each range from very little certainty of execution to absolute certainty. While the TSO would prefer absolute certainty of projects before eligibility for DS3 auctions or tariffs, to enable projects be developed and financed some flexibility on this is required.

Evidence of a signed grid connection agreement represents a significant investment by developers requiring the payment of a first stage payment. It provides a degree of certainty for the TSO while being early enough in the development process to allow developers to factor in potential system services revenues in their investment analysis. It is unlikely that some system service providers will be able to access project financing for new investment until after award of a system service contract. All costs incurred prior to being awarded a system service contract will be at risk. With the considerable uncertainty associated with winning a system service contract the greater the financial commitment required prior to the auction, as established by the qualification requirements, will increase the barrier to entry and undermine the capability of meeting the 2020 Renewable Targets with minimised levels of curtailment. It should be noted that discussion has commenced on the grid application process to follow on from Gate 3 which will be determined throughout 2016. It is possible that being able to contribute to the provision of system services could be considered as one of the criteria for access to the grid. Therefore IWEA proposes that further consideration be given to the interaction of the grid application process and the provision of system services and recommends engagement between the relevant workstreams in this regard.

In the area of planning, planning consent by an appropriate authority (albeit where appeals can still be raised) strikes the appropriate balance between providing absolute project certainty for the TSO and providing early enough investment clarity for a system service provider.

Question 15: Would your responses to Questions 13 and 14 differ with regard to Capacity plant? If so, please explain why.

In relation to Question 13 the answer would be the same. We would not see the same interaction between the grid application policy and capacity as may be possible with system services. It is likely that any plant which may deliver system service will also contribute to the capacity requirement.

Question 16: Do you agree with the example given above to identify emerging technologies?

IWEA believes that there should be no barrier to entry for emerging technologies and they should be able to compete with other technologies for the provision of services. The fundamental objective of the DS3 arrangements is to deliver the system services required to ensure the 2020 Renewable Targets can be achieved with minimal curtailment. The DS3 arrangements are not intended to support research and development although this may be an indirect result.

Question 17: Should the inclusion of emerging technologies be on a capped share, or reserved share basis?

See answer to Question 16. In the case where the provision of the system service has been clearly demonstrated there should be no need to cap or reserve the share from emerging technologies, however if the provision of services has not been clearly demonstrated, and there is a risk to delivery, a cap may be appropriate to ensure that there is still an adequate level of system services available.

Question 18: Is it appropriate to have similar limits on emerging technologies for the procurement of Capacity under the I-SEM. If so, is the above approach also appropriate for that procurement process?

Given the level of capacity currently on the system it does not seem necessary to include either of these limits for capacity.

Question 19: Do you favour a highly detailed assessment (Option A) above, or a lighter assessment with an increased reliance bid bonds, and on 3rd party assurance of bidder's data.

Whichever method is chosen, it is important to ensure that the system services are delivered. If the assessment is too onerous and acts as a disincentive for providers to participate then this will not deliver the services required. On the other hand if there is not adequate assessment the TSO runs the risk of the providers not actually being able to deliver the required services, which will then impact on system operation and the curtailment of wind energy.

Question 20 (13): Do you agree with the above outline of evidence and data?

IWEA agrees with the outline of evidence and data and the data provided in appendix 2. However, this is on the basis that access to appropriate contractors and consultants satisfies the requirements of the service provider having such the skills and expertise.

Question 21 (13): If you consider that Option B outlined above is a preferred assessment process do you believe that some of the criteria outlined in 5.11-5.13 should be utilised as the minimum criteria in this assessment?

The criteria outlined in 5.11 – 5.13 (Grid, Planning and Permits) are critical parts to any development project and so should be included in the minimum criteria for the assessment.

Question 22 (14): Do you consider the above qualification processes to be applicable for the CRM qualification process? What do you consider to be the main differences (if any) between DS3 System Service qualification and procurement and CRM qualification and procurement and how should these be addressed?

We consider the above qualification process to also be applicable for the CRM qualification process.

Question 23: Do you agree with the key principles to be considered by the TSOS when developing contracts for DS3 System Service procurement as outlined above?

In general IWEA supports the key principles outlined in the paper, however we have the following concerns:

- We welcome the minimum annual revenue requirement, however the certainty that this provides is somewhat offset by the provision for a claw-back in later years. This would raise concerns for equity funding in particular. The impact of other participants also needs to be considered. The mechanism effectively creates different prices for the same product for different parties. If top up payments are required for a single DS3 revenue pot are other participants disadvantaged because a scalar would be applied to all parties which do not have a minimum annual revenue requirement?
- There is still not sufficient clarity in relation to the use of scalars and we welcome the proposal for further consultation on this.
- In relation to lead times and key milestones, there needs to be protection against risks which are outside the control of the developer, such as later construction or commissioning of the grid connection. This requires further consultation.

Question 24: Do you believe there are other key criteria that should be included in contractual agreement between the TSOs and System Service providers.

Question 25: Which (if any) elements of the above discussion should also apply to the procurement of Capacity under the I-SEM?

Question 26: Do you agree that bid bonds and performance bonds are required, and the performance bonds should be at risk on the delivery of specific milestones?

IWEA supports a requirement to evidence substantial financial commitment to the development of the proposed system service this could be through the requirement to put in place bid bonds and performance bonds to ensure the delivery of the system service products. However these should be set at a level that does not create a barrier to entry for new participants, but that provides the correct incentive to deliver. The bonds should not be drawn down on if the reason for delay in delivery is beyond the control of the generator. We would envisage that the performance bond would replace the bid bond and that both would not be required at the same time.

Question 27: What are your views on the compatibility of existing bonding arrangements and those proposed for DS3 System services? Do you consider there is the possibility to align some of these to reduce the financial burden to market players?

This is something which could be further explored.

Question 28: To what extent would your responses to the above questions also apply (or differ) for the procurement of Capacity under the I-SEM?

The above responses should also apply for the procurement of capacity.

Question 29: Which of the above options do you prefer? Please provide a view of why you have chosen a particular option and the advantages your chosen option offers.

IWEA supports that Option 2 represents an appropriate balance between onerous requirements on both the service provider and the TSO, and early identification of projects which are not likely to deliver.

Question 30: Based on your consideration of options for the management of the build phase for DS3, do you wish to amend or augment your responses relating the management for build phase for new Capacity under the I-SEM?

Question 31: Do you agree that performance bonds should be set relative to the cost to consumers of any failure to delivery?

The level of the performance bond should be set such that it provides that appropriate incentive to deliver in a timely manner, without creating a barrier to entry for service providers.

Question 32: Do you agree that the level of performance penalty should vary inversely with the notice provided by the party that it will fail to deliver?

Question 33: Do you believe that these principles (relating to the level of performance bonds and penalties) should vary between DS3 and I-SEM Capacity?