Response: Electricity Support Schemes: Transitioning to I-SEM Arrangements

Proposed Decision Paper

About CEWEP

CEWEP is the umbrella association of the owners / operators of Waste-to-Energy Plants, representing approximately 400 Waste-to-Energy Plants from 18 European countries. Our members make up 86% of the Waste-to-Energy capacity in Europe.

CEWEP Ireland is the Irish branch of CEWEP Europe and has two members: Indaver, which operates the Meath Waste-to-Energy Facility and is proposing to develop similar facilities in Belfast and Cork; and Covanta, which operates the Dublin Waste-to-Energy Facility. By 2020 it is anticipated that members will have a total treatment capacity of over 1,070,000 tonnes per annum residual waste and export more than 90MW electricity and/or heat.

Introduction

The Department of Communications, Climate Action and Environment (DCCAE) is updating existing electricity support schemes supported by the Public Service Obligation (PSO) Levy (primarily for renewable energy) so that they are compatible with the new Integrated-Single Electricity Market arrangements (I-SEM) which is due to 'go live' in May 2018.

A balanced solution is being sought so as to ensure that the existing renewable support schemes are compatible with the new market design and operate efficiently. In this regard, CEWEP members are both subsidised under the Renewable Energy Feed in Tariff (REFIT) scheme in Ireland for the renewable fraction of their output power.

Capacity Payments

CEWEP members are concerned that REFIT's interaction with the Capacity Remuneration Mechanism reflects a downside risk to the subsidised energy from our plant with no corresponding revenue, and potentially the overall design impacts consumers of the Capacity Remuneration Mechanism (CRM) and Public Service Obligation (PSO) Levy more than it should.

This is in contrast to REFIT subsidised wind generation, which can choose not to qualify for a portion or all of the auction, and reduce the volumes procured (and potentially the clearing price in the auction) through non-participation.

Whereas a dispatchable REFIT generator must participate in the capacity auction for its full capacity, cannot formally withdraw from the auction, is exposed to potential penalties (with no capacity revenues, as these only reduce the REFIT compensation) and consumers procure more capacity than needed (as there is no reduction in the capacity volumes to be procured), potentially with a higher clearing price as a result.

This issue and a potential solution to the same has been previously highlighted by CEWEP in correspondence with the Department and therefore it is not proposed to reprise the matter in full in this response. However, for the sake of clarity and completeness, this previous communication is attached as an Appendix to this Consultation Response below.

Reference Price:

Choosing between Time-Weighted or Production-Weighted Production

The Department's Proposed Decision Paper considers that decisions in the paper should apply to co-firing or part renewables plant for the portion of their capacity that receives PSO levy support. CEWEP members consider that an alternative option as set out below should be given consideration.

Alternative to Choosing between Time-Weighted or Production-Weighted Production

Wind generation has been given an easier "reference price" in the blend of the Day Ahead Market (DAM) and the Balancing Market which recognises the balancing costs of wind generation in the Proposed Decision Paper. Moreover, this reference price will be calculated as the generation weighted average price (page 13 of the Decision paper).

Predictable generation (such as CEWEP members) will be given the time-weighted price as the target. The different technologies amongst CEWEP members likely leads to different levels of predictable output. Other non-wind technologies have comparable predictability issues.

As such, CEWEP members as producers of predictable generation would be held to a higher standard. It is submitted that all generation should be subject to the same standard and treated in an equivalent manner.

In the absence of any analysis of different technologies, it is further submitted that in holding non-wind generation to a different standard, this may be said to be discriminatory in nature.

Therefore, CEWEP proposes that in light of the above concerns, consideration should now be given to an alternative option of calculating the reference price on a generation weighted average basis in order to ensure that all generation is treated equally under the Proposed Decision process.

Appendix

23rd August 2017

Department of Communications,
Climate Action & Environment
29-31 Adelaide Road
Dublin
D02 X285

Dear DCCAE

On behalf of CEWEP, would like to draw your attention to an interaction of the proposed REFIT rules and the Capacity Remuneration Mechanism. We seek to agree an appropriate process with DCCAE (as owners of the REFIT scheme) and CER (as administrators of the REFIT scheme, and under its SEM Committee functions, owner of the Capacity Remuneration Mechanism). We are concerned that REFIT's interaction with the Capacity Remuneration Mechanism reflects a downside risk to the subsidised energy from our plant with no corresponding revenue, and potentially the overall design impacts consumers of the CRM and PSO Levy more than it should as well. This issue impacts all "conventional" REFIT generation participating in the CRM.

It is also important for CEWEP members to participate fully in the Capacity Mechanism for the brown non-subsidised output.

This overall situation is in contrast to REFIT subsidised wind generation, which can choose not to qualify for a portion or all of the auction, and reduce the volumes procured (and potentially the clearing price in the auction) through non-participation.

There are a number of routes, both in the operation of REFIT and the capacity market rules, which could improve the current situation. Nevertheless, we understand that there is limited action that can be taken under the capacity market process in the run-up to the first capacity auction. We would like to meet the CER/DCCAE as appropriate to discuss potential processes to ensure we are being appropriately incentivised in the round and fairly remunerated for those incentives.

Further detail is provided below.

Should the Department or the CER require any further information relating to these matters, CEWEP would be happy to provide the same. Alternatively, should a meeting be deemed useful this can be arranged at your earliest convenience.

Yours sincerely,

Jackie Keaney
President CEWEP Ireland

Background on CEWEP Members

CEWEP members comprise two operational conventional generation waste-to-energy facilities, both dispatchable market participants. Both are subsidised under the REFIT scheme in Ireland for the renewable fraction of their output power. Furthermore, there are plans for further development of new facilities, both in Ireland and in Northern Ireland. Any future subsidy regime for such new generators is currently unknown.

Capacity Market Rules - Obliged Mandatory Participation for Full Capacity

As the Capacity Market Rules currently stand for the existing generators, both generators must a) register under the Trading & Settlement Code to sell energy, and b) register Candidate Units under the Capacity Market Code. There is a further obligation to qualify those units for their full de-rated capacity for the auction. Furthermore, there is an obligation to submit a bid into the auction. For the avoidance of doubt, the registration of Candidate Units is automatic, and qualification and participation in the auction will happen automatically under standard processes at defined commercial rates, even if a participant does not directly engage with the Capacity Market Code process.

There are specific opt-outs for being allowed to bid a higher price and/or opt out of an auction entirely, but we do not believe we meet the criteria of the current capacity market code to meet these criteria.

REFIT and Capacity Revenue Interaction for Conventional Plant vrs Variable Plant

The direction of travel in the REFIT discussions is - correctly in our view - any Capacity Payment revenue earned by a subsidised generator must be taken into account in calculating (and reducing) REFIT subsidy to prevent double state aid subsidy.
A capacity market participant, however, which has received a capacity payment has:
a) All its energy revenues capped at a strike price, currently close to €500/MWh; and
b) Is exposed to a penalty payment linked to market prices when it fails to deliver energy or be deemed available for ancillary services during a high-price period.
It is proposed - by our understanding - that a) will be also considered in calculating REFIT subsidy, but that b), penalties which arise due to non-delivery will not be.

Correspondingly, there is no benefit in capacity market participation for a REFIT subsidised generator. Windfarms, for example, may choose not to participate in the capacity market auction. Their deemed capacity contribution is subtracted from the amount of capacity to be procured. Therefore, while REFIT payment to these generators will be higher, this will be offset by a lower volume of capacity procured (at potentially a lower clearing price) under the capacity market auction. All things being equal, an increase in the PSO Levy for Ireland consumers will be offset by a greater reduction in costs for the all-island consumer.

In general, however, a large dispatchable REFIT generator must participate in the capacity auction for its full capacity, cannot formally withdraw from the auction, is exposed to potential penalties (with no capacity revenues, as these only reduce the REFIT compensation) and consumers procure more capacity than needed (as there is no reduction in the capacity volumes to be procured), potentially with a higher clearing price as a result.

Further Complication for CEWEP Members

CEWEP members are only part subsidised for their electrical output. The capacity remuneration mechanism is an important part of the revenue for the non-subsidised output of the plant. Therefore CEWEP members have interest in earning capacity revenues for the brown portion of its output, but not its green portion of its output.

Furthermore, the REFIT scheme has had a history of pro-rating all revenues received (energy, capacity, constraint) over a PSO year between the green and brown elements of the validated renewable fraction. Therefore, if, for example, a CEWEP generator cleared only the "brown" proportion of its capacity, e.g. 45% of a 100MW machine, the capacity revenues (and presumably the penalties as well) will be allocated pro-rata between the green and brown revenues, i.e. 55% of the cleared 45MW revenues would be allocated to the green portion and would be lost, and only 45% of the 45MW of cleared revenues would be allocated to the brown portion of revenues. The generator would still be exposed to 100% of the penalties.

Proposed Adjustment to REFIT for I-SEM

CEWEP believes that:
a) CEWEP members should participate for their full capacity volume, and bid in seeking to secure capacity volumes as if the plant is fully non-renewable, i.e. it should <u>not</u> attempt to bid in the brown percentage of the capacity at a 'normal' price, and the renewable proportion of the capacity at a high price to only part-clear the auction.
b) Brown capacity revenues include the capacity revenue for the non-renewable fraction, less pro-rated-to-non-renewable-fraction proportion of a) any capping of the energy price and b) any non-delivery penalties.
c) REFIT includes the capacity revenue for the renewable fraction, and a) the capping of energy prices <u>AND b) the penalties for non-delivery of the REFIT proportion</u>, in the calculation of the REFIT support.

While REFIT will be exposed to the potential of capacity penalties, we do not believe this to be unduly discriminatory in favour of supported conventional generation (relative to supported variable generation) as:
1. Conventional generation, unlike renewable generation, has no choice but to participate fully in the auction
2. In the case of part-renewable plant, there is still an incentive to maintain reliable delivery of the full plant, as penalties for failure of delivery of the entire plant do apply to the brown revenues. (Specifically, we are not asking for the "first xMW" application of energy caps and capacity penalties to be covered preferentially by REFIT).

We believe that this is the simplest change which can be made to give clarity to part-renewable REFIT generators in the short term. It would be ideal if this clarity can be given well in advance of the capacity auction, in line with the wider discussion on REFIT.

We have considered but are not in favour of the following concepts, for the following reasons:
1. Consider capacity revenues as separate to the price of subsidised energy. This would allow the plant to keep all capacity revenues (and potential penalties), and REFIT subsidy would be calculated relative to the energy revenues only. We believe this would lead to the potential for double-state aid.
2. Price the green proportion of the capacity higher than the brown proportion of the revenues. The cleared proportion of the capacity (including all penalties) would be considered brown. This leads to artificial bid patterns in the capacity market, and the potential for the green proportion of the offer clearing (either due to a mis-forecast renewable percentage, or the higher capacity price inadvertently clearing the auction) would still need to be considered. In general, given the long lead times for future capacity auctions, any mechanism which relies on forecasting renewable fractions under the capacity auction is not favoured.

Potential Longer-Term Capacity Market Changes

We do not believe that there are any 100% renewable conventional generators under REFIT greater than 10MW participating in the first capacity auction.

In the future, it might be considered that all "Priority Dispatch" plants may choose not to qualify capacity under the Capacity Market Code; this is currently afforded to non-firm and variable generation currently, on the basis that their specific characteristics have higher risk than for conventional plants. This would allow fully renewable generators to opt out of the REFIT scheme, reducing the capacity target to be procured, and potentially delivering lower clearing prices. If that flexibility were offered, we would argue that fully renewable plants should be exposed to full capacity market penalties (as otherwise, there is zero incentive to be reliable for capacity), but the "**Proposed Adjustment to REFIT for I-SEM**" above should remain in place for part renewable plants (i.e. that REFIT covers the renewable fraction penalties). While it could be argued that part-renewable plant should not participate for their non-renewable fraction, this would be on the basis of forecasts.

We are not in favour of introducing new rules for a unit specific price cap to account for the different risk profile of subsidised plant in the future, as this has the draw-backs as described above.