



ELECTRICITY SUPPLY BOARD
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REGULATORY AFFAIRS

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25th September 2008

**ESB Input to consultation by the Northern Ireland Authority for
Utility Regulation on Key Issues in the Development of its 5 year Corporate
Strategy – June 2008**

Dear Mr. Sheils,

ESB welcomes the opportunity to comment on the above consultation. This is a valuable opportunity for stakeholders to contribute to the debate on the important factors affecting the electricity market in the medium term.

ESB operates in the electricity sector in Ireland, Northern Ireland and Britain and consequently has a clear interest in the work programmes of the NIAUR, the Commission for Energy Regulation and Ofgem.

The electricity sector in Ireland faces a difficult challenge over the coming decade to increase the penetration of renewables, whilst still ensuring a competitive market for investors and the lowest possible price for customers. It is therefore vital that careful, pro-active consideration is given to balancing the many issues, and the strategy consultation is an important component in this regard.

The response is split into two sections. Section 1 discusses general comments on the Corporate Strategy consultation and Section 2 details specific comments to the eight questions given in the paper.

If you have any queries regarding the points made in this response, please do not hesitate to contact me. We look forward to meeting with you on the 1st October.

Yours sincerely,

Niamh McCarthy
On behalf of ESB Regulatory Affairs
ESB

Section 1: General Comments

- The five year Corporate Strategy and recent NIAUR consultations on Sustainability and the Retail Market are interdependent, and the responses from these recent consultations will provide valuable input regarding the views of stakeholders on these issues in a medium-term context. ESB would welcome a consolidation of the views raised in these previous consultations into the next draft of the five year corporate strategy for further public consultation.
- Regulation of the All-Island electricity market relies on cooperation between the regulators of the Republic of Ireland and Northern Ireland. ESB recognise that the NIAUR are responsible for the protection of the Northern Ireland customer, however, it is important that the objectives of NIAUR's five year strategy are not significantly different to those in the CER's five year Strategic Plan. Given that the last CER Strategic Plan covered 2006 -2011, it would also be beneficial to work with the CER to align the planning horizons. It would be further advantageous if both the NIAUR and the CER would consider issuing a joint 5 year corporate strategy, addressing the specific issues affecting the development of the All-Island electricity market.
- The paper is comprehensive, however, we would suggest that in the next draft the explicit priorities associated with each individual sector are set out more clearly.
- The paper mentions that the NIAUR liaise with some other Departments, including planning, to offer a coordinated approach to strategy implementation. We would welcome further articulation of NIAUR's role in relation to these other government departments, as well as further details of coordination on a wider EU level.
- The following points summarise the issues which ESB feel are of importance within the five year horizon of the Corporate Strategy;
 - Harmonisation of transmission and distribution business processes and IT systems for networks
 - Collaborative role of NIAUR in the functional specification for SMART metering
 - Investigation into the effect of separate payment schemes for renewables (ROCs and Feed-in tariffs) in relation to the development of renewables on the system
 - Further examination of the support necessary to ensure large scale penetration of renewables
 - Incorporation of the results of the All-Island Grid Study into network development

Section 2: Specific Comments

Consultation Question 1:

Are there other significant challenges which NIAUR ought to have reflected in Chapter 3.1?

- ESB fully agree with NIAUR that sustainability and environmental issues will be the key challenges facing the NI electricity market, and in general the paper identifies all of the topical issues. However, some issues maybe more important than others in the near future, in particular, the role of renewables. Renewables, especially wind, has the ability to contribute to the solution of other key challenges (security of supply, cost of climate change/carbon), but their orderly interconnection and operation in the market needs to be carefully considered.
- The role of Research and Development and the investment required to deliver new solutions to the issues of security of supply and climate change should be recognised as a strategic challenge for the future. The NIAUR will have a key role to play in facilitating the timely deployment of new technologies and the development of policies which support investment in energy efficiency measures and alternative fuels.
- Another key challenge which should inform strategy is the requirement to ensure that investment in infrastructure and increasing energy demands can continue to be met. Competition for investment will mean that investors will weigh up the risks and opportunities associated with the regulatory environment before committing to new projects. The strategy should therefore address how investor confidence can continue to be supported.
- There will continue to be a major focus at European policy making level on energy market integration, security of supply and improved market competitiveness. The strategy process should also take into account of the challenges posed by the reform agenda and the broader societal goals which underpin them.

Consultation Question 2:

Are there other significant opportunities which NIAUR ought to have reflected in Chapter 3.1?

- ESB believe that the All-Island market framework offers both regulators the best opportunity to protect their customers.
- With regard to best regulatory practices, ESB would like to draw attention to the value of predictability in regulatory actions. Through regulatory stability, the NIAUR

can help ensure investor confidence in the market. Stability in the regulatory process in addition to well-signalled changes, allow current and potential investors to forecast risk more accurately and therefore minimise the cost of business.

- The opportunities offered by increased interconnection should be addressed in the strategy. What impact will it have on the SEM and do the regulators need to review its implementation in advance?

Consultation Question 3 & 4:

Are there additional significant “context issues” and/or “issues within context issues” which NIAUR ought to have reflected in Chapter 3?

ESB makes the following comments;

- Section 3.2 (i): Rising prices to consumers and the need for concerted action
 - It is unclear what influence, if any, the regulator can have on rising commodity prices. As a small economy, Northern Ireland is a price-taker and has no influence on world fuel prices.
 - This section covers rising fuel prices and mentions security of supply. We agree that geo-political and market events can have an effect on world commodity prices. However, we would suggest that since Ireland is a price taker in this regard, emphasis is placed on domestic security of supply.
 - The fourth paragraph begins “Our objective in electricity is to protect consumers’ interests, and in gas it is to promote the development of an efficient, economic and co-ordinated gas industry”. Why do the objectives differ? Given that the All-Island market is still in its infancy, it would seem hasty to assume that the objective in relation to gas does not apply to electricity.
- Section 3.2 (ii): All-Island energy developments

This section discusses market synchronisation. The All-Island market has been in operation since the 1st November 2007 however, there are possibly further ways in which the two markets could better operate as one.

- Currently, the ESB and NIE operate two different business process systems for dealing with the domestic and new connections market. It is possible that harmonising these systems will reduce the cost of doing-business in both markets, especially in relation to reducing the cost of entry into the market, since a new entrant is unlikely to consider the Republic of Ireland or Northern

Ireland in isolation. A study of the value of harmonisation in this area should be considered.

- Additionally, an investigation into the effect of the differing payment schemes for renewables (ROCs and Feed-in tariffs) could be useful. Currently, the divergence in the value of ROCs and Feed-in tariffs acts as a financial incentive to locate windfarms in Northern Ireland. If these payments were harmonised, investment would more likely take place where it is most strategically beneficial from a system perspective, instead of where it is possibly more financially beneficial to do so.

The impact of the current regime should be examined and evaluated against the cost of windfarm development as set out in the All-Island Grid Study, which endeavoured to find the least cost solution to renewables penetration.

- Section 3.2 (v): Environmental Sustainability
 - ESB has submitted a response to the Sustainability consultation and incorporates those comments by reference into the Corporate Strategy consultation
- Section 3.3: Some initial thoughts on other long-term influences

ESB agree with NIAUR that energy issues must be considered in a long-term context and welcome the opportunity to discuss certain issues.

- In our Corporate Strategy, ESB has committed to operating 800 MW of wind capacity by 2020. In this respect, ESB consider the work undertaken in the All-Island Grid Study to be of great value. The Study concluded that to incorporate 6,000 MW of wind onto the system will require significant network re-enforcements. This is a primary pre-condition. ESB are committed to investing €11 billion in network infrastructure by 2020. To create the most efficient system and to facilitate the resolution to network congestion, ESB would like to see an All-Island approach to network investment.
- ESB believe that if the All-Island system is to accommodate up to 6,000 MWs of wind, back-up generation in the form of fast-response plant, such as OCGTs, will be required. Currently, Eirgrid and SONI are working to harmonise ancillary services and are considering the inclusion of a fast-response payment. ESB supports this approach.

Consultation Question 5:

Are there other significant “wholesale” issues which NIAUR ought to have reflected in Chapter 4?

Overall, we feel that the conversation regarding security of supply, high and volatile fuel prices and liquidity of contracts, would be better served taking place within the context of the SEM.

- Section 1(b): High and volatile fuel costs

ESB agree with the NIAUR that renewable energy offers one solution to exposure to high wholesale prices since domestic renewables are a hedge against rising imported commodity prices. Renewables also offer a certain amount of security of supply by diversifying the generation mix. However, renewables alone will not be sufficient and additional fossil fuelled generation will be required to meet expected demand. For this reason, the risk associated with high and volatile wholesale fuel costs cannot be fully diversified. In light of this, it is important that the market should be left to operate on free market economics, where investors are left to decide on the most efficient and economic solution. Any superfluous regulation in a deregulated market only increases the regulatory risk for the investor, and thus the end-price for the consumer.

Regulatory certainty and stability are among the most powerful tools at the disposal of the NIAUR to best ensure a fair wholesale price. Other methods include ensuring a fair and transparent market for all investors, by reducing any instances of inequality in the market. The on-going work on All-Island Ancillary Services harmonisation is a noteworthy example.

Consultation Question 6:

Are there other significant “network” issues which NIAUR ought to have reflected in Chapter 4?

- Section 2(c): The future direction of “all-island” energy work (network issues)

ESB fully support the work by the NIAUR and the Commission for Energy Regulation to create a fully integrated and harmonised All-Island market and ESB agree that Networks will play a key role in the development of the All-Island market. In this regard, ESB would like to make four points:

1. The business processes and systems employed by ESB and NIE to deal with domestic customers and new connections presently differ. This has two effects, first from the perspective of attracting competition this divergence acts

as a possible barrier to entry. It is likely that a new entrant would prefer to enter both markets simultaneously. Second, it is possible that by adopting the same systems, the overall cost of providing the networks service may be reduced.

2. Currently, ESB are involved in the roll-out of SMART Metering, which is anticipated to cost between €0.6 and €1 billion. This requires the development of a functional specification. This is being conducted without the inclusion of Northern Ireland. To minimise customers' current and future costs, it could be more beneficial if this initiative was conducted on an All-Island basis. Additionally, this point also applies to Smart Grids in relation to sustainability.
3. A consensus on the meaning of SMART Networks and SMART Metering and the benefits and costs associated with them must be studied further.
4. We concur that the NIAUR will need to liaise with other government departments, in particular Planning Consents and Policy. ESB believe that network development needs to become more pro-active, anticipating where improvements will need to be made. Again, this is something that applies to the All-Island transmission system and would benefit from an All-Island perspective. The All-Island Grid Study identified three main regions where significant re-enforcements would be required; Cork/Kerry, Mayo/Sligo, Donegal. These proposals need to be supported and implemented as appropriate.
5. The ability to deliver investment in a timely manner and in the volume required to meet renewable targets is a major concern for Network companies

Consultation Question 7:

Are there other significant "retail" issues which NIAUR ought to have reflected in Chapter 4?

ESB has submitted a response to the Retail Market Consultation and incorporates those comments by reference into the Corporate Strategy consultation.

- The importance of price signals to modification of customer behaviour should be understood and acted upon if renewables targets are to be achieved

Consultation Question 8:

NIAUR would welcome early views from respondents on the urgency, importance and thus prioritisation of strategic goals and work priorities.

The NIAUR state that their role is “to protect the interests of the consumers of electricity.....by promoting effective competition”.

ESB believe that the most efficient way to promote effective competition is through the operation of the All-Island market and furthermore, by ensuring a level-playing field for all market participants within the market, in as many areas of operation as possible.

The following points identify issues that ESB feel are of particular importance within the 5 year horizon of the Corporate Strategy, in no particular order;

- Harmonisation of transmission and distribution business processes and systems for networks
- Collaborative role of NIAUR in the functional specification for SMART metering
- Investigation into the effect of separate payment schemes for renewables (ROCs and Feed-in tariffs) in relation to the development of renewables on the system
- Further examination of the support necessary to ensure large scale penetration of renewables
- Incorporation of the results of the All-Island Grid Study into network development