

# **ESB Corporate Response to Draft Forward Work Programme April 2011 – March 2012**

## **Executive Summary**

ESB welcomes the publication by the Utility Regulator of its Forward Work Plan for industry comment.

ESB requests the Utility Regulator to consider the proposals and recommendations made by it in this response including:

- Timely conclusion and implementation of the outcomes of the review of market power and liquidity, in particular with respect to the removal of ring-fencing restrictions, in order to best facilitate sustainable retail competition for the benefit of all customers;
- Assessment as to whether customer switching thresholds can be revised upwards in advance of delivery of the enduring solution for the retail market in Northern Ireland;
- Holistic assessment of the impact of renewables on the remuneration of all generators combined with the development of appropriate flexibility incentives in order to reduce regulatory risks;
- An increased focus by the Regulatory Authorities on Regional Market Integration beyond those changes required to ensure compliance with the EU Congestion Management Guidelines;
- In advance of the commencement of RP5, the finalisation of an agreed plan and process for achieving the renewables trajectory;
- Leveraging strategic direction (where appropriate) and synergies from the decisions made in Ireland in the overall Smart Grids area;
- Development of policy to support Clean Coal and Carbon Capture & Storage technologies for the island of Ireland.

ESB believes that regulatory action in these areas will further promote competition in the retail and wholesale markets, advance regional market integration, support improvements in security of supply as well as leverage progress in Smart technologies in an all-island context.

ESB believes that such actions in combination with other activities incorporated in the FWP are appropriate for the period April 2011 – March 2012 and will further support the development of competitive electricity markets and the power system.

## **Introduction**

ESB welcomes the opportunity to respond to this consultation and provide its views on the Utility Regulator's Forward Work Programme (FWP) covering the period April 2011 to March 2012. The paper provides insight into those areas that the Utility Regulator considers will require the greatest focus over the coming year and provides early insight into anticipated priority issues for the following year.

ESB had responded to the previous Forward Work Programme for 2010-2011 and appreciates that some of the priority areas that it had highlighted at that time have been included in this FWP.

In this response ESB has structured its comments primarily in relation to the electricity sector and focusing on the following key areas:

- Retail Market Competition;
- Competition in the SEM;
- Regional Integration;
- Sustainability & NIE T&D Price Control;
- Security of Supply;

### ***Retail Market Competition***

While domestic market opening was completed in November 2007, the level of customer switching has been restricted somewhat due to lack of systems infrastructure. It will be important that significant regulatory focus is given to support timely completion of the enduring solution for electricity switching so that it can be operational no later than May 2012.

In advance of that, it is appropriate for the Utility Regulator to review whether both the overall interim customer switching threshold of 125,000 customers can be increased and the monthly switching level of 7,500 increased so as to provide additional opportunities for customers in advance of the enduring solution being delivered.

In addition to changes to the interim switching infrastructure arrangements, ESB suggests that there may be lessons to be learned by the Utility Regulator from the retail market competition experiences and regulatory challenges that have arisen for Ireland. There is significant retail competition in the domestic sector in Ireland. The pace of evolution of this competition necessitated a change in regulatory controls on ESB Customer Supply. This resulted in a switch away from a K-Factor regulatory approach to a Maximum Allowed Revenue (MAR) approach with such arrangements to apply until the market share levels prescribed in the CER Retail Roadmap have been achieved, after which price-controls on ESB's Supply business will cease.

It is anticipated that ESB Customer Supply will have achieved the prescribed market share levels by early 2011, after which the MAR controls will end. This will in theory allow full tariff freedom for ESB's Supply business in Ireland. However, the fact that ESB's Supply business is still currently subject to ring-fencing restrictions from

ESB's Generation business, significantly impacts on its ability to most effectively and economically manage its market risks. This separation is driving and will continue to drive unnecessary duplication and transaction costs which are being passed to customers through end-user tariffs. These costs, which could be avoided by the removal of these ring-fencing restrictions, when included in ESB tariffs are providing additional headroom for rival Supply Companies who use ESB tariffs as the price-to-beat in their customer offerings. This situation does not offer best value to customers and is hindering ESB's ability to offer competitive tariffs to all sectors of the retail market.

NIEES is likely to find itself in a similar position, to that of ESB Customer Supply, when the pace of domestic competition increases in Northern Ireland, and the K-factor regulatory approach becomes impractical. ESB suggests that the Utility Regulator considers in the near term what the most appropriate balance between regulatory controls, ring-fencing and monitoring arrangements required to support sustainable retail market competition will be for all Suppliers including the incumbent supplier in Northern Ireland. The consultation on Market Power & Liquidity grants the opportunity for an early regulatory decision in this respect, which will provide the foundation for sustainable competition in the interest of all customers in Northern Ireland and at an all-island level.

### ***Competition in SEM***

ESB welcomes the proposed initiatives of the Utility Regulator through close working with CER to ensure effective operation of the SEM. ESB believes that the Bidding Code of Practice and monitoring of the application of this code by the MMU are the operative controls that minimise the potential for market power abuse.

ESB notes the Utility Regulator commitment to work with CER to implement any necessary changes arising from the review of market power and liquidity in the SEM. ESB has previously made proposals to the SEM Committee in relation to progressive deregulation of the SEM. As part of these proposals ESB has provided a commitment to the Regulatory Authorities in relation to wholesale market liquidity on the proviso that it is granted vertical integration. This liquidity proposal recognises that Directed Contracts which were initially imposed with the primary intent to limit the incentive for abusing market power, have additionally become important for market participants in terms of risk management.

ESB believes that appropriate steps taken subsequent to the review of market power and liquidity will provide the opportunity for the development of increased competition in both the wholesale and the retail markets (as outlined above). ESB calls on the Utility Regulator and CER to leverage this opportunity to establish sustainable competition for the benefit of all customers on the island of Ireland.

The integration of a high level of renewables within the SEM generation portfolio has impacted on the operation of the market and the financial returns of all generators whether conventional or renewable in nature. There are a number of fundamental consultations ongoing at present including those of Scheduling & Dispatch, Capacity

Payment Mechanism, Treatment of Losses as well as further work on harmonisation of Ancillary Services.

It will be essential for the future stability of the wholesale market that these four areas are looked at in an holistic fashion to ensure that all generators operating in the market can be sufficiently rewarded for their past investments. In addition, ESB suggests that further consideration be given to an incentive based mechanism, geared towards conventional generation plant for the significant flexibility of operation that they provide. This flexibility is required in order to facilitate increased intermittent generation onto the power system. The TSOs have previously considered that this flexibility service may have merit, yet it has so far not appeared on any work plans. In the absence of the suggested holistic assessment and incentive mechanisms, the level of commercial and regulatory risk may be to a degree that deters future investment.

### ***Regional Integration***

Regional Integration could provide a number of benefits including facilitation of renewables and increasing wholesale market competition. The introduction of intra-day trading arrangements between SEM and BETTA and further with North Western Europe will provide increased opportunity for market participants to balance their market positions closer to real time reflecting the increased variability of renewables on the power system, and also provide the opportunity for increased contract liquidity.

Regional Integration with Great Britain and Europe was recently highlighted by the Northern Ireland Regulator at the Energy Northern Ireland conference, as being of greater importance than minor modifications to the existing SEM. However, this importance is not evidenced in the Regional Integration actions for 2011-2012 and 2012-2014 as listed in the work programme.

It will be important that the Utility Regulator and CER proceed with the delivery of those changes to the market rules and systems to ensure initially, compliance with Congestion Management Guidelines and then subsequent to that, implementation of the EU Target Models for Forward, Day Ahead, Intraday and Balancing arrangements. ESB calls for greater focus within the FWP on Regional Integration as it believes that the industry as a whole would benefit from increased initiatives in this area.

### ***NIE T&D Price Control, Smart Grids and Sustainability***

The recently published DETI Strategic Energy Framework for Northern Ireland 2010 aims to decarbonise Northern Ireland's electricity supply as far as practicable. This framework commits Northern Ireland to achieving 40% of its electricity consumption from renewable sources by 2020, a significant increase from the 10% level that exists today. This framework recognises that on-shore wind currently offers the most cost effective means of renewable electricity generation delivery for Northern Ireland. The DETI Framework also recognises the value that Smart Grid technology implementation will provide towards the development of a flexible smarter grid in the longer term.

The Utility Regulator will, during 2011, be preparing for the NIE T&D Price Control which will cover the period from April 2012. Achieving DETI Smart Grid vision, energy efficiency and renewable energy targets will collectively require significant capital investment in the T&D networks including on the broader smart technologies. As such, it will be essential that RP5 provides sufficient cost recovery and incentives to ensure that the required investments in Northern Ireland's networks, both to support new and refurbishment of old, can be and will be made. However, there will be significant commercial, technical and delivery risk on NIE, associated with roll-out of the necessary transmission and distribution network infrastructure, should RP5 be finalised in the absence of an agreed plan and process for achieving the renewables trajectory. ESB suggests that the FWP be updated to include development of a viable plan for delivery of the 40% renewables target.

In addition, ESB suggests that there may be synergies to be gained at an all-island level, by leveraging from the strategic direction and choices already made in Ireland in the overall Smart Grid area. Such synergies would include those in support of electrification of transport, which is one of the transformations that DETI recognises in its Strategic Energy Framework.

The CER has made significant progress in its Smart Metering programme and has also recently conducted a consultation on Demand Side Management. It may be cost effective for the Utility Regulator to consider using the work and outputs of both of these initiatives as the baseline for strategy in these areas for Northern Ireland. This would most likely lead to wider interoperability and greater opportunities of scale which could drive overall implementation efficiencies in retail electricity markets and energy services delivery at an all-island level.

### ***Security of Supply***

The Regional Market initiative and delivery of the DETI renewable targets will contribute to security of supply. Smart Grids, Energy Efficiency and Demand Side Management will also have a role to play in this area. As mentioned previously, there will be merit in the Utility Regulator considering the outcomes of the CER consultation on vision for Demand Side Management and leveraging all potential synergies in support of supply security on an All-Island basis.

ESB supports the Utility Regulator plans to develop long-term arrangements for security of supply in conjunction with CER, DETI and DCENR on an all-island basis. ESB believes that all forms of low-carbon generation should be considered, recognizing that technology advancement will occur as the pressure to find global solutions to carbon emissions intensifies over the coming years. ESB believes that Clean Coal and Carbon Capture and Storage (CCS) will have a significant role to play and suggests that the Utility Regulator, where appropriate in conjunction with CER, progresses the development of policy to support the utilisation of these technologies. It should be noted that it is not only coal fired generation that will require CCS. If the Electricity Sector is to be fully decarbonised between 2030 and 2050 then CCS on Gas Fired generation will also be required.

Completion of the North-South Interconnector will also support security of supply on an All-Island basis. It may be necessary for the Utility Regulator and CER to work closely with the TSOs to ensure progression of this project through to construction stage, and thereafter with the transmission asset owner to support the completion of construction and commissioning of this critical infrastructure. The FWP could benefit from inclusion of activities to promote the necessity and benefits of this infrastructure within both jurisdictions.

### ***In Summary***

ESB welcomes the publication by the Utility Regulator of its Forward Work Plan for industry comment. The work-plan is extensive and challenging for 2011-2012 and ESB recognises that as other priority issues arise over this period that this plan may need to be refined in line with resource and budgetary considerations.

Nonetheless, ESB would ask the Utility Regulator to consider the proposals and recommendations made by it in its response to this consultation, in particular:

- Timely conclusion and implementation of the outcomes of the review of market power and liquidity, in particular with respect to the removal of ring-fencing restrictions, in order to best facilitate sustainable retail competition for the benefit of all customers;
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