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## Possible Cancellation of Generating Unit Agreements in Northern Ireland

Dear Kenny,

Thank you for giving SSE the opportunity to comment on the Utility Regulator's consultation paper on the possible cancellation of Generating Unit Agreements (GUAs) in Northern Ireland.

SSE is a utility with both generation and supply interests in Ireland. As SSE Airtricity we supply more than 180,000 electricity customers in Northern Ireland. To secure energy for those retail customers, SSE is involved in electricity generation and energy portfolio management. Our wholesale business priorities are competitiveness, sustainability and flexibility.

### Cancellation

Based on the economic and policy assessment contained within the consultation paper, **SSE would agree with the Utility Regulator's decision to instruct the cancellation of the two remaining GUAs in December 2014.** We have not attempted to critique the detailed economic analysis of their ongoing value to consumers, other than to note the sensitivity of the evaluation to forward fuel and carbon prices<sup>1</sup>. Nevertheless, the existence of the GUAs (mis)allocates some significant risks to consumers in Northern Ireland.

We would make the following comments on some of the policy considerations covered in the consultation paper.

### Market Redesign

The paper states that:

*"We consider that the continued existence of the GUAs may also make implementation of any new market arrangements more complex. However, it could also be argued that the*

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<sup>1</sup> The analysis used data on forward fuel and carbon prices taken from the ICE, taking an average of the prices over the period 28<sup>th</sup> October to 1<sup>st</sup> November. Forward prices have seen a significant shift already, with European storage levels at their highest point in 5 years.

*existence and continuation of the Generating Unit Agreements may act to mitigate any uncertainty that could arise as a result of introducing a new market design.”*

Given that a number of options for the high level design could radically change participation (particularly bidding behaviour) in the market, SSE would agree that preserving the GUAs could pose difficulties during the implementation of iSEM arrangements. Far from mitigating uncertainty, the continuing existence of the GUAs may serve to reduce the availability of private capital to the market as a whole under new trading arrangements.

Detailed forecasting of market revenue will also be more sensitive to the performance (and incentivisation) of PPB, making it more difficult to draw a conclusion on whether to cancel the GUAs. In a more actively traded electricity market, risk and incentive would more naturally sit with the asset owner.

### **Contract Liquidity**

The paper states that:

*“There are both risks and benefits associated with cancellation in relation to contract liquidity. On balance, we believe that any cancellation decision should not have any significant negative impact on contract liquidity but that cancellation may improve liquidity in the market.”*

SSE would agree that the cancellation of the GUAs should actually serve to improve liquidity in the market. At present, a substantial volume of the NDCs on the OTC platform (relative to generation market share) have been provided by AES. With a larger independent gas and coal generation portfolio in the SEM, we would expect offerings on the OTC platform to increase by a similar or greater amount than PPB NDC offerings would decline.

### **Market Power**

The paper does acknowledge that both all-island and Northern Ireland HHIs would increase on cancellation of the GUAs. We would point at the ACER paper on configuration which notes that:

*“Locational market power is inherently present in the electricity market, regardless of the zonal or nodal design. This is because some generators and loads are inherently more suitable to solve congestion in specific locations in the network. Nevertheless, locational market power can be mitigated to some degree. In the case of smaller zones or nodal pricing, ex-ante remedial actions are more likely replaced by market mechanisms, solving congestion based on bids from all generators in, for example, the day-ahead market. This way, the generator with locational market power is faced with more competition in solving the congestion.”*

Assuming that:

- The existing SEM bidding zone configuration is retained following review, and;
- Sufficient market power mitigation measures are included in iSEM design.

SSE cannot see a market power issue arising as a result of the cancellation of the GUAs. However, these are relatively large caveats, and NIAUR should ensure that the iSEM Project Team has a clear indication of the final decision before the trading arrangements are finalised.

### Security of Supply

The analysis of Security of Supply is peremptory:

*“We do not consider there to be any security of supply issues arising from either cancelling or not cancelling any of these contracts. We have considered the likely revenues which each unit will earn in the SEM and concluded that market exit is unlikely in the medium term.”*

SSE would suggest that the medium term outlook for these units will be dependent on the repair of the Moyle Interconnector, the solution to Eirgrid’s tender **‘Provision of Local Reserve to Mitigate the Impact of Local Electricity Transmission Constraints from 1 January 2016’**, the redesign of the trading arrangements<sup>2</sup> and operational performance<sup>3</sup>, all of which are difficult to include in an economic model.

However, in the long run, SSE would suggest that the Security of Supply criteria is better served in an environment in which the final GUAs are cancelled. Currently, risk is misallocated to customers, distorting incentives and providing a barrier to market entry.

### Concluding remarks

Customers would be better served by the cancellation of the two remaining Generating Unit Agreements for effect in December 2014. However, given the level of recent and historic volatility in inputs, a Time Series analysis of forward fuel and carbon prices may be useful. If you have any questions with regard to our response, don’t hesitate to contact me.

Yours sincerely,

Connor Powell  
**Market Development, SSE (Ireland)**

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<sup>2</sup> This is particularly true with regard to the design of any Capacity Remuneration Mechanism.

<sup>3</sup> Sunk assets are not free of operational risk, as experience with the Moyle Interconnector illustrates.