

**TYNAGH ENERGY
L I M I T E D**

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20th May 2016

Ref: TEL/CJD/16/083

RE: Consultation on DS3 System Services Interim Tariffs

Dear Sirs,

Alongside the answers to the questions raised in this consultation TEL would like to draw further attention to areas both within this consultation and in the wider DS3 process.

The fundamental point of DS3 is to maximise the benefit to consumers from the high levels of wind capacity on the island, which requires significant and timely investment primarily from thermal generators. This investment will only happen if there is a supportable investment case. Without this, investment will not occur and the DS3 project will not succeed.

TEL would like to raise the following points in response to the DS3 system services consultations to date:

1. Continual reduction in incentive to invest
2. Interim Tariff Rates
3. Payment Basis – dispatch only
4. Capacity Payment Effect
5. Overall Revenue and Volumes

1. Continual reduction in incentive to invest

DS3 has been in planning since 2010. In the early discussions, it was reported that there would be in the region of €600 million available to investors, since then (and particularly in the last year) there has been a continual diminution of potential return to investors.

By 2013 the TSO recommended¹ a fund of €355 million to pay for these essential services, while the Decision² in 2014 settled on €235 million which was based on sharing the value of the return between generators and the consumer. The justification for this does not take into account the benefits to the country of the reduction in costs / fines to Ireland in failing to meet its EU 2020 targets. This would increase the value of DS3 by €120 - €600 million per year³.

¹ DS3: System Services Review TSO Recommendations 2013

² DS3 System Services Procurement Decision and Emergent Thinking (SEM-14-108)

³ The Draft Bioenergy Plan, DCENR 2014, EPA March 7 2016



Since then the Competition Metrics Consultation has emphasised that generators may only get a long term contract for some of the services that they can offer. If a service fails the competition test, generators will not be able to get a long term contract for that service.

The Scalars Consultation and in particular the Volume Scalar has outlined that generators may not be paid at the regulated tariffs for services (if there is excess volume), while the Auction Design has created uncertainty as to the levels of risk that will be placed on a generator.

This latest consultation has further undermined the investment case as these proposed Interim Tariff Rates will see a loss of income for many generators. Existing HAS rates have fallen, while the new services may see a net loss (between DS3 and Capacity) to many generators. Finally these Interim Tariffs will only be paid to those generators who are physically despatched, as opposed to those who would be technically realisable (as in the Decision). This is of particular importance to TEL as the plant is frequently on in the market but not despatched. Under the HAS arrangements, Tynagh loses out on ancillary services whenever it is constrained off. The Decision stated that this would be rectified under DS3.

2. Interim Tariff Rates

Interim tariffs have to be set at a level that will encourage new entrants and investment. Investors look at these rates as indicative of future long term income for the provision of DS3 System Services. If these rates are too low, investment will flow elsewhere.

The published Interim Tariffs may actually see a loss of revenue for generators. Of the fourteen services, three fast acting services have been placed into an experimental pot of €3 million. The remaining four new services which appear to have been budgeted to receive more than €20 million will see a matching reduction (as outlined in the consultation) for generators in their capacity revenue. While the initial seven services will actual see a drop of 24% in generator revenue for these services.

The following table outlines the current and proposed rates and shows the volume that will be provided by a 400MW CCGT with AVR providing Grid Code requirements.

	Volume	Proposed Revenue p/h	Current Revenue p/h
Primary Operating Reserve (POR)	20	€49.40	€47.20
Secondary Operating Reserve (SOR)	20	€27.40	€45.40
Tertiary Operating Reserve (TOR1)	32	€38.08	€60.48
Tertiary Operating Reserve (TOR2)	40	€39.60	€37.60
Replacement Reserve – Synchronised (RRS)	200	€26.00	€42.00
Steady State Reactive Power - Leading	158	€31.60	€44.24
Steady State Reactive Power - Lagging	248	€49.60	€69.44

The HAS services were being paid out of a pot of €52 million in 2015 for security of supply and to support an SNSP of 50%. Since then the SNSP limit has increased however there is an effective reduction in value for existing providers of between 20 – 24%.

3. Payment Basis – dispatch only

The Decision Paper continually refers to DS3 commencing in 2016 and that DS3 will be paid irrespective of constraints on the better of a generators market or dispatch position.



However, this paper states that the Interim Tariffs will only be paid for dispatch. There is nothing in the decision paper to suggest a different payment basis for the Interim period.

This minded to position of paying purely on a dispatch basis for the interim period adds further doubt to an investment case and there has been no justification given for this divergence from the decision.

4. Capacity Payment Effect

The consultation references the elephant in the room, that the rates for the new services will effectively be balanced by similar reductions in capacity payments to generators. This is because the Capacity Payment calculation is based on the BNE. This BNE will be a peaker. This peaker will be able to provide RM1, 3 and 8 when offline (the vast majority of the time). This peaker will consequently earn more from these DS3 services than any other generator on the market. This increase in DS3 revenue (for the virtual plant) will therefore lead to a matching reduction in the capacity payment for that plant. However this reduction in capacity will lead to a disproportionate reduction for every other generator in the market.

5. Overall Revenue and Volumes

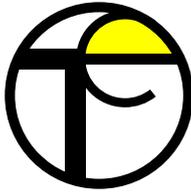
The consultation states that “the total payments for the existing seven HAS services should at least be the same as in the HAS arrangements”. There was a marginal change in the rates between 2014/15 and 2015/16. The total payments for each of the existing services are not available for 2015/2016 but are available for 2014/2015⁴. These show a total payment of €48 Million for these services. Using the rates for this year it is possible to calculate the volumes for this year.

HAS Service	14/15 Cost	HAS Rates	Volume
POR	€5,997,822	€2.34	2,563,172
SOR	€8,961,140	€2.24	4,000,509
TOR1	€8,941,887	€1.87	4,781,758
TOR2	€5,373,694	€0.93	5,778,166
RRS 1	€2,656,983	€0.20	13,284,915
RRD 1	€5,313,966	€0.54	9,840,678
Reactive Power Lagging	€7,230,863	€0.13	55,622,023
Reactive Power Leading	€4,153,649	€0.13	31,951,146
Total	€48,630,004		

Effectively, Volume (14/15) = €48 Million / Rates (2014/2015)

Using these volumes in conjunction with the proposed Interim Tariff Rates it is possible to calculate a total payment for the existing 7 HAS services. This results in an approximate drop in payments of 20% to €40 million as per the following table.

⁴ Ancillary Services Report Eirgrid November 2015



DS3 Service	14/15 Volume	DS3 Rates	Cost
POR	2,563,172	€2.47	€6,331,034
SOR	4,000,509	€1.37	€5,480,697
TOR1	4,781,758	€1.19	€5,690,292
TOR2	5,778,166	€0.99	€5,720,384
RRS	13,284,915	€0.13	€1,727,039
RRD	9,840,678	€0.64	€6,298,034
SSRP	87,573,169	€0.10	€8,757,317
Total			€40,004,797

(SSRP rate has been reduced based on an assumed RP factor of 0.5)

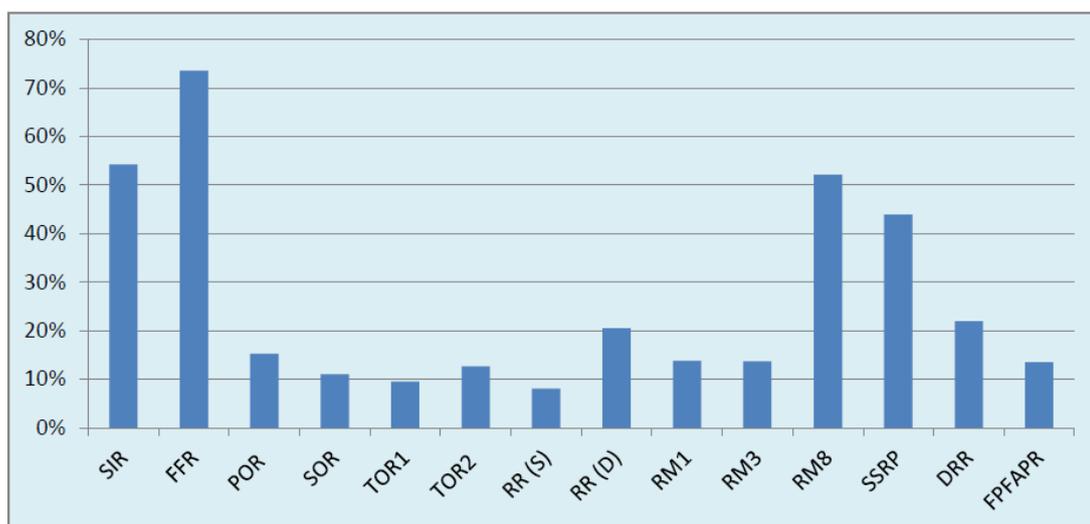
The consultation states that there will be no change in the overall payment from these services, therefore it implies that there has to be an increase in the volumes, it is possible to calculate these assumed new volumes.

Volumes (16/17) = €48 Million / Rates (Interim Tariff)

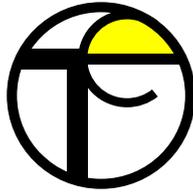
In order to maintain the same total payment across the seven services as stated in the consultation there would need to be an increase in the volumes of approximately 20%.

The 2014 Decision Paper outlined an estimate of the shortfall for each of the services. The average required increase for each of the seven HAS services is less than 17%. Considerably less than the increase of 20% that would be needed to ensure that the payments under the Interim Tariffs would meet those of the HAS services under the 2014/2015 rates.

Figure 4: Required Increase in Installed Capability to Achieve SNSP of 75% under the Selected Scenario



Finally in point 59 of the Decision, it states that the expenditure cap will rise incrementally from its current level of €60 million to €235 million in line with the delivered volumes. If the delivered volumes for these services are already going to be supplied in 2016 / 2017 then the rates should meet the expected regulated tariffs for these rates in 2020.



Either there is an expected increase in volumes in which case there should be a significant increase in the budget for these services or there is no increase in volumes in which case in order for the total payment to remain the same the rates cannot be decreased.

If you have any questions regarding any of these comments or our answers to the specific questions please do not hesitate to contact me.

Yours sincerely,

A handwritten signature in black ink that reads "Cormac Daly". The signature is written in a cursive style and is positioned above a solid horizontal line.

Cormac Daly
Risk and Regulatory Manager