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Dear Martin,

Implementing the European Electricity Target Model in Great Britain – ESBI response

ESB International (ESBI) welcomes the opportunity to comment on Ofgem's open letter on implementing the European Electricity Target Model in the British market. As the first few Network Codes coming out of the Third Package come towards the end of the drafting process, it seems a timely point to consider the practical implications for the British market arrangements and the changes proposed under the Electricity Market Reform (EMR).

ESB International

ESB International (ESBI) brings together our worldwide generation, engineering and related services businesses.

ESBI has been a developer and operator of independent Combined Cycle Gas Turbine (CCGT) generation projects in the GB market for almost 20 years. We own, operate and trade Corby power station and developed the 850MW plant at Marchwood, which was commissioned late in 2009. We are also at an advanced stage with our latest 860MW development at Carrington which is intended to become operational early in 2015. Additionally, we own and operate the 406MW Coolkeeragh plant in Northern Ireland. We are developing further large-scale CCGT projects at other locations across GB, including our early-stage 1500MW project at Knottingley, West Yorkshire.

In addition to increasing our conventional generation fleet, we continue to grow our position in the UK

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wind market. Our operational and development portfolio will be around 165MW, comprising of: the 24MW West Durham Wind Farm in Northern England; the 20MW Hunters Hill; and 15MW Crockagarron projects in Northern Ireland. Additionally, we recently completed commissioning of England's largest onshore wind farm, at 66MW, at Fullabrook in Devon and we have recently started construction of our 38MW Mynydd y Betws Wind Farm in South Wales. We are also active in the ocean energy sector.

Increases in physical interconnection, in particular the commissioning of the East-West interconnector later this year, coupled with the further development of the regional market, our operations in Ireland will become increasingly linked with the GB market.

Summary of views

In the current period of uncertainty and structural change in our market, it is timely that Ofgem have decided to examine the implications of the European Target Model for GB, and we welcome this consideration as being of great importance. The ongoing Network Code process arising from the European Third Package will result in legislation that will take precedence over our national laws and regulations; as such the question for GB is perhaps not one of implementation of the Target Model but rather of adaptation to ensure our current and proposed market codes are compatible with pan-European rules.

During a time of significant reform – both actual and proposed – it is necessary to ensure that changes are as enduring as possible in the interests of stability and investor confidence. The scale of change currently envisaged – from both domestic projects such as EMR and Project TransmiT, and the pan-EU Network Codes – is not conducive to a stable and secure market. However, we believe that with coordination and cooperation it will be possible for Ofgem, DECC, and industry participants to work through the changes and minimise disruption.

For example, EMR is likely to introduce a Capacity Mechanism to the GB market. Whilst the Target Model is silent on the use or form of Capacity Mechanisms, it is important that their design and compatibility with neighbouring markets is considered to ensure efficient market coupling and the optimal use of interconnectors, as intended in the Target Model.

Responses to questions

1. What are the key aspects of the Target Model for GB?

The creation of GB Hub and market coupling will be a change for our market. However, we feel it is important to recall that none of the aspects of the Electricity Target Model, aside from balancing, mandate participation from the market; it is therefore important to ensure that day-ahead liquidity on the Hub does not become a panacea to cure perceived market deficiencies. To this end, transparency is extremely important in what the day-ahead price is being used for, and what that usage is trying to achieve. We appreciate the importance of a strong reference price for the introduction of the capacity market; however it is important that day-ahead liquidity is not promoted at the expense of liquidity further out along the curve. This longer-term liquidity is extremely important as an investment signal for the generation that is required to ensure security of supply.

It is also extremely important that any changes in the GB market balancing arrangements – for example as a result of the current Significant Code Review (SCR) on electricity cash out pricing – are aligned with the Network Codes. The Framework Guidelines on Balancing, for instance, are suggesting the mandating of a cleared marginal price, rather than pay-as-bid; the SCR process must take this strongly into account.

Market splitting, while a potential aspect of the application of the Target Model to the GB market, is not a necessity for compliance with the Network Codes. It is extremely important therefore that clear, comprehensive and transparent consultation is a part of any change process, and that adequate consideration is taken of neighbouring markets and the wider implications of creating different price zones. Should the GB market be split, the zones must take into consideration internal as well as regional issues, be a fair reflection of costs and create no impediment to the development of market coupling and the price benefits that should accrue.

2. What changes will be needed to GB market arrangements?

The Capacity Allocation and Congestion Management (CACM) Network Code currently released by ENTSO-E for consultation covers the day ahead and intraday elements of the Target Model. It, and the other elements of the Target Model, has broad similarities with the existing GB market arrangements, and as such we do not expect that significant change should be necessary provided that internal GB reforms

are not in conflict with the Target Model.

The creation of GB Hub, already underway, is a sensible move at this point in time; however, as mentioned, it is imperative that the day ahead market does not become the focus for all available liquidity. Emphasis on one section of the Target Model in this way could impact on the overall structure of the market and therefore impact forward investment signals for the significant amount of generation that is required in the medium term. .

It is possible for the GB market, within the Target Model, to retain its current principles of self-dispatch and self-balancing. No changes, whether the implementation of European Regulations or domestic reform, should restrict market participants' ability to make market-based choices.

3. Should we try and minimise change or consider holistically the best combination of GB and EU requirements?

Change is coming, both from the EU Network Code process, and internally from changes to GB market arrangements; it may not be possible to minimise change. It is, however, sensible to consider the huge amount of change that is taking place in the market in a holistic manner. It is particularly important, given the lesser influence that GB holds over European policy than over our own, that changes implemented in the GB market do not conflict with EU Regulations.

An important area for Ofgem to consider is the change process of the Network Codes; we are aware that ACER is undertaking work in this area and would emphasise that the GB industry needs to be kept abreast of developments in these efforts. The status of the Network Codes as legislation and the need to change them via the Comitology process is a concern which we appreciate cannot be removed; however greater clarity in the change process would be warmly welcomed as a means of extending an element of stability in a time of change and investor uncertainty.

In addition to the work being carried out centrally in Europe it is extremely important to be aware of reforms and changes undertaken by our neighbouring Member States. Although not mentioned directly in Ofgem's letter, the results of the recent consultation issued by the Irish Single Electricity Market (SEM)

Committee regarding the implementation of the Target Model in their market should be taken into consideration. One option being discussed by the SEM is the potential of a form of an expanded BETTA to create an All-Islands Market under the same market rules; if this option were taken forward, entry would take place by end 2016. The GB market should consider such an eventuality, as well as the potential effects and benefits of other options being considered by the SEM, which with increased interconnection may have an affect on market arrangements.

Rather than making a choice between minimising change and considering requirements holistically, ESBI believes that Ofgem should consider all changes holistically as the surest way of minimising disruption.

4. How can we deliver the best outcomes?

There is a potential disconnect between the draft Network Codes consulted on with industry and the final Code that is released after the Comitology process. We appreciate that this may be a concern for Ofgem in ensuring GB market reform is in line with Network Codes such as CACM, which are not currently finalised. However, we believe that as the principles of the internal single market for electricity have already been agreed, it is best to ensure that all proposed GB requirements are in line with the Target Model.

In order to achieve this there should be an EU compatibility check, with GB reforms compared to, and brought into line with, the Target Model. Proactively corresponding with the broad line of change in this way will allow GB to maintain greater stability in the market and more enduring reform than becoming vulnerable to the necessity of reactive market ‘fixes’.

5. What process is needed to take this work forward?

We believe that, where the issues interact, domestic GB reforms should consider the European angle as a matter of course, and that this should be made explicit in industry consultations. Further, we would welcome cooperation between those working on different reforms and consultations within GB which have implications for the single European market – for example between this consultation and the current Ofgem consultation on Integrated Transmission Planning and Regulation – to ensure that overlapping and interlinking issues are dealt with in a coordinated manner. This should ensure that domestic modifications to market arrangements remain compatible with the Target Model.

Should you have any queries regarding the responses in this letter, or wish to discuss anything further, please do contact me at the address below.

Yours sincerely,

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