Single Electricity Market

(SEM)

Decision on Supplementary Consultation Paper on modified and combined Modifications to Facilitate Delivery of Capacity

SEM-23-101

30th November 2023

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1. Introduction

There have been a number of proposed CMC modifications raised which relate to difficulties which CRM auction winners are facing in meeting key deadlines, such as meeting the Substantial Financial Completion (SFC) Date or the Long Stop Date. In addition, other CMC or TSC modifications have sought to address the impact of delays on financial viability, including indexation proposals and proposals aimed at reducing the potential impact of contract erosion.

In SEM-23-001 the SEM Committee approved a modification containing elements of some of the CMC modifications raised to mitigate the impact of a Third-Party Judicial Review or Third-Party Planning Appeal. The modification allows for the SFC and Long Stop Date to be extended by a period equal to the Third-Party Extension Period where that Capacity Market Unit is subject to a Third-Party Judicial Review or Third-Party Planning Appeal. The participant may also seek the approval of the RAs to extend the Capacity Quantity End Date and Time by a period no greater than the Third-Party Extension Period, to mitigate the impact of contract erosion.

There have been a number of other proposed modifications which relate to other causes of delay potentially faced by the winners in recent auctions, such as delays in the delivery of grid and/or gas connections or extraordinary supply chain events.

In SEM-23-080, published on 6 October 2023, the SEM Committee recognised that Capacity Market Units which have been successful in recent auctions face a variety of significant challenges in delivering contracted capacity. In this consultation paper, the SEM Committee also stated that:

- Whilst there may be merit in a more permissive approach to handling delays, there are a number of flaws in the industry's outstanding proposals;
- The industry's current "ad-hoc" approach of proposing individual Modifications which seek to define *ex ante* the types of events which would merit automatic extensions of the SFC Date and/or Long-Stop Date will not appropriately address all the issues and will not optimally deliver CMC objectives;
- Rather than approving a series of CMC/TSC Modifications which seek to define *ex ante* the circumstances which will lead to the grant of extensions, the SEM Committee is considering implementing more generalised provisions in the CMC

which will include provisions for the SEM Committee to grant extensions on a case-by-case basis, as and when market participants apply for extensions to the Substantial Financial Completion date, the Long-Stop Date, and the Capacity Quantity End Date and Time.

In SEM-23-080 the SEM Committee consulted on two modified and combined CMC modifications to deliver a more cohesive overall approach to managing risks associated with delivering multi-year New Capacity. The proposals are summarised in Section 2 below.

2. Summary of Consultation Proposals

SEM-23-080 set out proposals for the two following modified and combined CMC modifications:

- Modification 1: Linking approval of Substantial Financial Completion Delays to Long Stop Dates and Capacity Quantity End Date and Time for specific auctions;
- Modification 2: Providing a mechanism for the SEM Committee to approve extensions to the Long Stop Date and Capacity Quantity End Date and Time for specific auctions.

Under both modifications, the SEM Committee would consider applications for extensions on a case-by-case basis and grant extensions only where consistent with the objectives of the CMC, when the market participant has justified the request with robust evidence and where the extension would otherwise be consistent with the SEM Committee's statutory duties.

Modification 1: Linking approval of Substantial Financial Completion Delays to Long Stop Dates and Capacity Quantity End Date and Time for specific auctions

This first Modification will ensure that where the SEM Committee considers that an SFC extension is appropriate in light of CMC Objectives and the SEM Committee uses its powers to grant an SFC extension to multi-year New Capacity, there will be a mechanism within the CMC for the SEM Committee to consider a commensurate extension to the LSD and to the Capacity Quantity End Date and Time, should this be sought.

The Modification aims to reduce the risk to investors that a new CMU can meet its extended SFC Date, but decides to terminate rather than proceed to SFC because either the developer:

(a) cannot deliver in time to meet the original Long Stop Date, because of delays in achieving SFC; or

(b) can still meet the Long Stop Date, but the impact of contract erosion means that the project is no longer financially viable.

The SEM Committee would review applications on a case-by-case basis, and approve extensions which are consistent with CMC objectives.

SEM-23-080 proposed that only multi-year New Capacity contracts would be able to apply for extensions to the SFC Date, Long Stop Date and the Capacity Quantity End Date and Time. SEM-23-080 also consulted on whether the modification should apply only to capacity which was awarded in specific auctions or have a “sunset” clause.

Modification 2: Providing a mechanism for the SEM Committee to approve extensions to the Long Stop Date and Capacity Quantity End Date and Time for specific auctions

The second modification aims to mitigate risks that materialise after SFC has been achieved. For instance, suppose that an investor is in a position to achieve SFC by the original SFC Date, so has no need to apply for an SFC extension. However, the investor still faces risks that if it proceeds to sign contracts, some other risk which crystallises after SFC has been achieved, with the result that either:

(a) The new CMU fails to meet the Long Stop Date; or

(b) The delay in achieving completion is such that contract erosion occurs to such an extent that proceeding with the project is no longer financially viable.

This second Modification aims to mitigate risks that appear post-SFC, by providing a mechanism for investors to apply to the RAs to obtain extensions to the Long Stop Date and the Capacity Quantity End Date and Time, even after SFC is achieved.

As with the first Modification, the SEM-23-080 proposed that only multi-year New Capacity contracts would be able to apply for extensions to the SFC Date, Long Stop Date and the Capacity Quantity End Date and Time under this second Modification. This Modification proposal is not intended to completely remove delivery risk from the investor – if delays are extensive and are such that other solutions are likely to better achieve CMC Objectives (such as deliver capacity earlier), extensions may be limited.

SEM-23-080 also consulted on whether this second Modification should also apply only to capacity which was awarded in specific auctions or have a “sunset” clause.

3. Summary of Consultation Responses

3.1 Responses

The SEM Committee received fourteen responses to the consultation (SEM-23-080), three of which were marked as confidential. The non-confidential responses were from:

- Castlelost FlexGen Ltd.
- Bord Gáis Energy
- Bord na Mona
- Energia
- ESB GT
- EirGrid/SONI/SEMO
- FERA
- Mutual Energy
- Powerhouse Generation Ltd.
- Shannonbridge Power B Ltd.
- SSE

3.2 Overview

Of the respondents, the majority broadly supported the proposals. In particular, the proposals were strongly supported by the majority of investors awarded contracts in the 2024/25 T-3 auction and the 2025/26 T-4 auction.

Responses supporting the modification proposals generally expressed a desire for both proposals to be implemented in tandem and were in favour of the proposed case-by-case assessment for granting extensions. BGE wrote that allowing delays due to third parties would result in a better outcome for consumers and in terms of the carbon cost when compared to the alternative of procuring Temporary Emergency Generation.

Amongst market participants:

- Energia were opposed to the proposals, which they argued were retrospective.
- SSE argued in favour of the five modifications raised by market participants due to issues including extraordinary supply chain disruptions, gas connections and grid connections, and felt that it was important to maintain the distinction between

delays which were due to third-parties and delays which are the responsibility of the developer.

Some respondents commented further on certain aspects of the proposals, which are discussed further below.

EirGrid/SONI were opposed to the proposals. They advised that modifying key aspects of the Code, such as the risk allocation model, should only be done following more detailed engagement with the System Operators, adequate consultation, robust analysis and detailed design.

The main areas raised by respondents are summarised below.

3.2 Applicability of modification proposals

Contract length

A number of respondents, principally representing DSUs, including FERA, expressed the view that the modification proposals should be applied to contracts of all lengths, i.e., one-year contracts, should be included.

Auction specificity

ESB GT questioned the rationale of applying the second modification proposal to specific auctions only as third-party delays can occur in many situations. Bord na Móna similarly argued that the proposals should apply to all auctions, perhaps subject to a "sunset" review, while BGE also favoured a "sunset" approach. SSE also raised questions regarding the linking of the proposals to specific auctions and stated that there should be an effective date set instead. The TSOs expressed their view that, if progressed, the modifications "should not be unnecessarily complex or discriminatory and apply to all who may avail of it at the effective date".

Connection-related delays

SSE argued that connection-related delays are not an activity that developers can affect and that due to the large demand for connections at present, there must be a mechanism within the CMC to extend the SFC date, the Long-Stop Date, and the Capacity Quantity End Date and Time for connection-related delays.

Mutual Energy noted its view that proposed modifications regarding delays caused by gas connections have been too open-ended and could weaken incentives for developers to undertake proper due diligence and build sufficient time into their project plans.

3.3 RA assessment process

BGE requested that the RAs provide a set of non-exhaustive guidelines to provide transparency to investors on the assessment process for extensions. It also expressed its view that the RAs should clearly explain their reasoning for either approving or rejecting an extension request, and that guidance on the 'burden of proof' is needed.

The TSOs also called for remedial actions to be implemented in a way that is "almost automatic". The TSOs also noted that the proposals may introduce "a significant administrative burden in assessing applications", in the absence of "clear triggers and criteria". The TSOs also noted their concerns that it may be difficult to compel third parties to provide evidence and engagement, particularly if disagreement arises as to the cause of a delay.

Energia stated that it is important that the SEM Committee reach and publish the case-by-case decisions in a way that "facilitates transparency, competition and no undue discrimination". Energia requested that the SEM Committee specifies the criteria for granting an extension in the CMC.

Castlelost FlexGen Ltd and Shannonbridge Power B Ltd. stated their support for a case-by-case approach to granting extensions and viewed that this approach fulfilled the objectives of the CMC.

3.4 Timeline for delivery of capacity and extension length

A number of respondents commented on the implications of the proposals for the established lead-in times for delivery of capacity (i.e., a maximum of 48 months as is the case for T-4 auctions). ESB GT noted this current maximum timeline and argued that it does not align with the degree of complexity in the commissioning of new generation capacity. It pointed to the example of Poland, where 60 months lead-in time is provided.

Meanwhile, the TSOs argued that the introduction of broad application remedial actions could be regarded as acknowledgement that the current T-4 timeframes are "inadequate" for the delivery of new capacity.

In contrast, BGE viewed the T-4 lead time to be sufficient to deliver capacity and that therefore the financial incentive for capacity developers to deliver their projects on time must be maintained. However, BGE considered that the RAs should take a "permissive approach" in particular for those who may see delays in T-3 projects resulting in delays for T-4 projects.

In terms of the length of extensions provided, SSE argued that if extensions granted are insufficient for external delays to be resolved, the modifications will fail to solve the issue. Bord na Móna asked whether there would be any mechanism for market participants to query a SEM Committee decision to grant a shorter extension than requested.

3.5 Financial Commitment and Penalties

According to Bord na Móna, the consultation paper did not sufficiently address the "very large financial commitments" required, in particular in terms of SFC, "which is relatively early in the project implementation". In their response, Bord na Móna also commented that if the SOs were to propose termination of the Awarded New Capacity for not achieving SFC and the delays were not attributable to the market participant (i.e., were third party delays), performance securities should not be used and termination liabilities should be waived.

In contrast, the TSOs cautioned that relaxing the commitment model carries "additional risk of delayed delivery of capacity". The TSOs suggested that the SEM Committee consider "if additional commitment, in the form of performance securities, should be a factor in granting extensions".

Energia highlighted a recent report published by the Association for the Co-operation of Energy Regulators (ACER) which found evidence of "the benefits of well-designed, non-delivery penalties to ensure developers have the right incentives in place to ensure their capacities are delivered on time." Energia argued that "rather than allowing unrealistic developments to terminate", the proposals "extend their deadlines for delivery", which may "encourage less robust offers in the future".

3.6 Qualification process

ESB GT welcomed the proposed modifications but noted that there is a need to balance "a more permissive approach to delays in delivery" with "strengthening the application of the qualification criteria". According to ESB GT, this would help avoid projects becoming reliant on the potential for delays to be granted.

Mutual Energy noted that there is "no requirement on developers within the Capacity Market Code to engage with the gas TSO about a connection before prequalifying for a capacity auction", which puts pressure on timelines, particularly in Northern Ireland according to Mutual.

3.7 "Retrospective" changes

Energia stated that it opposed "modifications that are retrospective in effect" and considered that changes made after auctions are unfair as market participants may have made different decisions had the changes been in place before the auction.

3.8 Moral hazard and incentives to deliver

Energia argued that the proposed modifications may significantly change the delivery risks of the current T-4 2027/28 auction, the bidding behaviour of participants and may encourage less-prudent bids, i.e., create moral hazard.

The TSOs also argued that changes may weaken incentives to deliver capacity and/or lead to riskier projects being put forward and cautioned against the use of a more permissive approach to extensions.

SSE also argued in favour of extensions being linked to a third-party cause, which would reduce moral hazard.

3.9 Wider review and consultation

While the TSOs noted that they were not in principle opposed to the introduction of targeted remedial actions, they were concerned that the modification proposals would increase the risk of non/delayed delivery. The TSOs called for the RAs to "engage with the System Operators and other key stakeholders in relation to a larger programme of work which would provide a firm foundation for significant change", rather than what they viewed to be "piecemeal" changes. It should be noted that the TSOs have also opposed the individual CMC Modification proposals put forward by market participants with respect to a range of third-party delays, such as those relating to electricity and gas connections, and to general supply chain issues.

Energia and the TSOs noted the short consultation period and criticised the lack of legal drafting published alongside the consultation. Energia called for a CMC Workshop to be held before any progression of these modifications.

A number of other respondents expressed a desire to see CMC Modification drafting as a matter of priority.

4. SEM Committee Responses

The SEM Committee recognises that the majority of market participants support the CMC Modifications and see the need to de-risk delivery of projects in the current environment.

One respondent argued in favour of moving forward with the existing CMC Modifications proposed by industry, which focus on identifying a range of third-party delays, and only allowing extensions where there was a clearly attributed third-party cause but guaranteeing that New Capacity would be allowed extensions equal to the full duration of the third-party delay. This party's argument, and the arguments that have been made in favour of the range of outstanding third-party CMC Modifications, are predicated on the assumption that it is relatively easy to use independent expert determination to apportion blame in instances relating to delays under contracts between the developer and electricity / gas TSOs. However, the SEM Committee has received testimony that there are a range of legal and practical difficulties in using independent expert witnesses to determine fault attribution, including the time typically taken for independent expert determination. Whilst the SEM Committee does not rule out the use of expert independent witnesses in making decisions, the SEM Committee does not consider that it is feasible to make independent expert determination a mandatory and integral part of the process, or that it will be possible to make a binary decision on fault attribution in all relevant cases.

The SEM Committee has considered the arguments raised by one respondent in relation to retrospectivity. It is satisfied that the proposed Modifications will not operate retrospectively. As with the indexation modifications (see SEM-23-045), the proposals do not seek to reopen settled transactions.

The SEM Committee recognises the TSOs' concerns with respect to changing the risk allocation model, and that there are concerns with respect to moral hazard, with the risk of encouraging riskier projects to seek to Qualify for auctions. However, the SEM Committee notes that the TSOs are required to make an assessment of the deliverability of projects seeking to Qualify for an auction, and should screen out projects where it is not considered feasible for them to deliver by the first day of the relevant Capacity Year. Furthermore, under both modifications, requests for extensions would not be granted automatically but considered by the SEM Committee on a case-by-case basis and only granted where consistent with the objectives of the CMC, when the market participant has justified the request with robust evidence and where the extension would otherwise be consistent with the SEM Committee's statutory duties. The SEM Committee notes ESB GT's concerns that it may be appropriate to strengthen the application of Qualifying criteria.

The SEM Committee notes that even where the SEM Committee agrees to extend the Capacity Quantity End Date and Time, the investor remains strongly financially incentivised to deliver the contracted capacity as soon as possible, since in net present value terms, the value of a payment in Year 11 of contract is significantly less than the value of an equivalent cash payment in Year 1 of the contract.

The SEM Committee remains committed to the view that these provisions should only be applied to multi-year New Capacity and should not be applied to single year New Capacity. Single year New Capacity, if delivered late, will miss the key winter peak, so will have limited capacity benefit. As capacity payments are paid at a flat rate throughout the year, the likelihood is that late single year capacity will be paid at the flat rate in later, summer months when capacity has less value. Multi-year New Capacity, even if it misses the first winter peak, may deliver significant capacity value – value which it may not be easy to replace – in time for the second or subsequent winter peaks.

The SEM Committee notes that a number of market participants are seeking greater clarity as to how the SEM Committee would make extension decisions, possibly including issuing guidelines for investors. The SEM Committee recognises investors' desires for greater certainty, and directs interested parties to the Section A.1.2 of the CMC, where the CMC Objectives are set out. As stated in SEM-23-080, the SEM Committee will evaluate the advantages and disadvantages of extensions with reference to CMC Objectives. The SEM Committee recognises that some respondents are seeking more detailed guidance on how the principles set out in Section A.1.2 of the CMC may be applied in practice and the SEM Committee have asked the RAs to consider whether/how respondents' requests can be reasonably accommodated, via more detailed guidance, without fettering the SEM Committee's discretion to appropriately apply the CMC objectives in what may be a wide range of different circumstances.

Notwithstanding the fact that it may not be possible to issue much more detailed guidance, it is worth noting that the application of the CMC Objectives is likely to lead to a less permissive approach to extensions where:

- Applications are made close to the start of the first Capacity Year, and particularly where applications are made after the start of the first Capacity Year. It is important to maintain the incentives to deliver capacity in a timely manner, and to notify relevant authorities of likely delays earlier rather than later; or
- Delays are extensive and there are more options to source alternative capacity.

The SEM Committee recognises that a number of market participants have requested that more information is published after decisions have been made about the extensions and the reasons for the extensions, to aid transparency. The SEM Committee has asked the RAs to give due consideration to this issue, and work with the TSOs to publish appropriate information. However, the SEM Committee recognises that any additional requirements to publish information should be consistent with any existing obligations (e.g., REMIT) and should not duplicate any existing requirements. Furthermore, it may be appropriate for some information to remain confidential.

The SEM Committee recognises the mixed views on the issue of whether to strengthen or relax termination payments and performance securities with some (Bord na Móna) arguing in favour of relaxation, whilst others (the TSOs, Energia) arguing against. The SEM Committee continues to recognise the importance of balancing the financial incentives to deliver with the risks of deterring investors from exposing themselves to delivery risk, some of which may be outside their control. The SEM Committee continues to keep this issue under review, and to consult on the level of termination payments and performance securities prior to each auction.

The SEM Committee notes that some respondents have argued in favour of having auctions more than 48 months in advance of the start of the Capacity Year, and that having auctions further in advance would reduce the likelihood of delays. A number of the key projects where delays are currently being experienced relate to contracts awarded in the 2024/25 T-3 auction, which took place two and a half years before the start of the Capacity Year or the 2025/26 T-4 auction, which took place three and a half years before the start of the Capacity Year. The SEM Committee has already taken steps to increase the lead time between auction and the start of the Capacity Year to a full four years, and the effects of these changes in mitigating delivery risk have yet to be felt. There is scope within the existing CMC definitions to increase the lead time for T-4 auctions to as long as 54 months, and the SEM Committee intends to further review the lead-in times for auctions with a view to giving investors more time to develop projects.

5. SEM Committee Decisions

The SEM Committee has decided to implement both CMC Modifications set out in SEM-23-080, i.e.:

- Modification 1: Linking approval of Substantial Financial Completion Delays to Long Stop Dates and Capacity Quantity End Date and Time for specific auctions; and
- Modification 2: Providing a mechanism for the SEM Committee to approve extensions to the Long Stop Date and Capacity Quantity End Date and Time for specific auctions.

Both Modifications will apply only to Multi-Year New Capacity. The SEM Committee has decided that the Modifications will apply to auctions with capacity delivering from Capacity Year 2024/25 onwards. This will include auctions due to take place in 2024. The SEM Committee has taken this decision in recognition of the consideration that many of the factors contributing to delays at present are unlikely to recede in the short to medium term. For auctions held after 2024, the SEM Committee will consider whether these Modifications continue to be appropriate. In addition, as signalled above, the SEM Committee will reflect on the lead-in time for auctions and whether longer timeframes are feasible.

Under both modifications, the SEM Committee would consider applications for extensions on a case-by-case basis and grant extensions only where consistent with the objectives of the CMC, when the market participant has justified the request with robust evidence and where the extension would otherwise be consistent with the SEM Committee's statutory duties.

Any New Capacity awarded in the 2024/25 T-3 or 2025/26 T-4 auctions, which was granted an extension to the SFC Date prior to these CMC Modifications coming into force, but has not yet achieved SFC prior to this CMC Modification coming into force, will be able to apply for an extension to the Long Stop Date and the Capacity Quantity End Date and Time commensurate with the extension granted to the SFC Date, provided they do so within [20 days] of this Modification coming into force.

The SEM Committee will assess whether to approve each application on a case-by-case basis, in the light of CMC objectives. The SEM Committee will give due consideration to whether to publish guidelines for investors on what factors it will take into account in making these decisions. The SEM Committee will give further consideration to what information it is appropriate to publish in relation to extensions, and who should be responsible for publishing it, taking into account, inter alia, factors such as existing REMIT requirements and any legitimate confidentiality concerns.

6. Next Steps

The RAs are setting out the policy decision in regard to the two Modifications proposed in SEM-23-080 in the present decision paper. The legal drafting reflecting this policy decision will be published shortly. These Modifications will be applied in accordance with CMC B.12.11.4, which states:

The Regulatory Authorities may make a Modification that is different (including one that is materially different) from that proposed in a Modification Proposal, Workshop or consultation notice if the Regulatory Authorities are satisfied that, having regard to the issue or issues that were raised by the Modification Proposal, that the different Modification will or is likely to better contribute to the achievement of the Capacity Market Code Objectives.

The RAs will work with the TSOs and other relevant stakeholders to identify whether any consequential changes are required to the TSC with a view to implementing them in time to support settlement of the contracts.