Reserve Capacity Mechanism Working Group

Minutes

Meeting No.

of total capacity so that members can assess the significance of the issue.

		The Chair observed that there would be winners and losers. It seemed that good performance would be rewarded, potentially getting more money than they paid, whereas bad performance would still be exposed to refunds. Mr Geoff Down observed that the proposal seemed to indicate that the value of capacity was different according to the time at which it was running. He noted that this seemed to contradict the original principle of all capacity having the same value, which the working group had agreed to. Mr Thomas responded that capacity does have the same value however, the only way to test if a piece of equipment would deliver that value was to test it and apply refunds. Mr Huppatz and Mr Stevens noted that the proposal would not address the issue of unfair reward to generators that had a low capacity factor as well as low utilisation. They noted that it would be unfair to reward generators, such as peaking units, that have very low utilisation, at times when another generator goes on a Forced Outage. At such times, the risk is increased for generators that are running; and so it would be unfair to reward generators that are available but not running. Mr MacLean also echoed this concern. Mr MacLean queried whether the proposed refund mechanism would apply to Demand Side Programmes as well. Mr Thomas responded that his analysis was based on the scenario where harmonization had already been applied and DSP's would have unlimited availability. Mr Justin Payne observed that the proposal did not address the concerns raised about plants that have high Planned Outage rates such as 30% or above, indicating that they are unavailable for a long time but would still get paid rebates. Mr Huppatz noted that there were current provisions in the Market Rules that allowed System Management to reject Planned Outages and generators would be exposed to refunds thereafter. Discussion ensued whether the proposal created incentives for generators to be available. Mr Huppatz argued that currently there is a strong incentive to conduct planned maintenance to avoid Forced Outages. Mr MacLean added that in his opinion the incentive was not strong enough. He further added that this proposal would warrant renegotiation of contracts because currently the retailer pays for the cost of refunds that generators and DSPs incur. In the case of this proposal, the money and the risk would get reallocated implying that a renegotiation of those contracts would have to take place. The Chair also added that the situation would be worsened for Market Customers if a capacity shortfall occurred and the IMO was forced to recruit Supplementary Reserve Capacity. Mr Brendan Clarke queried how Intermittent Generators would be treated under this proposal. Mr Ruthven noted that a Facility would be eligible for a rebate in a Trading Interval in which it was potentially liable for a refund. Given that the Reserve Capacity Obligation Quantity of Intermittent Generators is zero, they would not be eligible for rebates. Members also discussed the impact of the proposal on DSPs. Mr Zammit noted that there was an outstanding action item on harmonization related to defining the conditions in which DSP could be dispatched.	

	Mr Thomas concluded by noting the three main points of concern that were raised by members in response to the dynamic refunds proposal: a) The need to renegotiate bilateral contracts b) The reallocation of money from Market Customers to Market Generators c) The continued application of costs of Supplementary Reserve Capacity to Market Customers Mr Huppatz added that further analysis should be done on the impact on different generating plants utilising different technologies because in his opinion, the technology of a plant can affect its Outage rates. The Chair suggested that it would be useful to use last year's data to conduct analysis of the impacts on each individual generator. The Chair queried if members were comfortable with pursuing this proposal albeit with further analysis conducted on the concerns raised by members. Mr MacLean mentioned that he was not convinced that this proposal would produce any significant incentives. His suggestion was that this proposal should not be pursued further. The Chair responded that it might be premature to dismiss this proposal without doing further investigation into its merits and demerits. *Action Point:* *The Lantau Group to address the following specific concerns raised by members on the proposed refunds mechanism:* *a) The need to renegotiate bilateral contracts* *b) The reallocation of money from Market Customers to Market Generators* *c) The continued application of costs of Supplementary Reserve Capacity to Market Customers* *The Lantau Group to conduct further analysis on the impacts of the proposed refunds regime on individual Facilities.*	
4.	**RESERVE CAPACITY PRICE (WORK STREAM 1)** The Chair invited Mr Thomas to make his presentation. The following discussion points were noted: Ms Yang mentioned that the quantity of excess capacity was a concern. The concern stemmed more from an economic efficiency perspective because excess capacity indicated inefficient over-investment. She also noted that the Shared Capacity Cost was always borne by the Market Customers, irrespective of whether there was excess capacity or a shortfall. Mr Tan noted that Mr Thomas's proposal was based on an implicit assumption about the price of reserve capacity in bilateral contracts. He added that a retailer would be in a better position if most of its capacity was bilaterally contracted, if the contract price was lower than the Reserve Capacity Price. There was some discussion around the nature of bilateral contracting, spigot control mechanism and the potential for introducing auction. Members also discussed the existence of	

market power and its interaction with the excess capacity problem.

Discussion ensued on the proposed 110% of MRCP and -3.25 slope. Members also discussed the potential impact of the reduction in MRCP that might come about due to revisions in the Weighted Average Cost of Capital (WACC).

At this point, the Chair invited Mr Ruthven to present the analysis on MRCP with the revised assumptions. He highlighted that this MRCP was only calculated for purely theoretical purposes and should not be taken as the real, binding MRCP for next year. Mr Tan clarified with Ms Yang what the impact of a revised debt risk premium might be on the MRCP.

The Chair concluded that more analysis was needed in terms of the impact of the RCP parameters on the market as it currently stands. He further added that the working group members needed to decide whether a strong case for change to the recommended proposal could not be made. If that was the case, then the working group might consider seeking further advice from the Market Advisory Committee and the IMO Board on whether a more radical approach to the RCM should be examined. The Chair also added that the next RCMWG meeting should focus on working out these issues and recommending a way forward.

Action Item:

> *The Lantau Group to examine the effects of the Reserve Capacity Price proposal with the help of some worked6(2)7.3)oCneakikikikikikikikikikikikTT*