ELECTRICITY ASSOCIATION OF IRELAND

Market Design Flagship Study: Recommendations for the Retail Sector

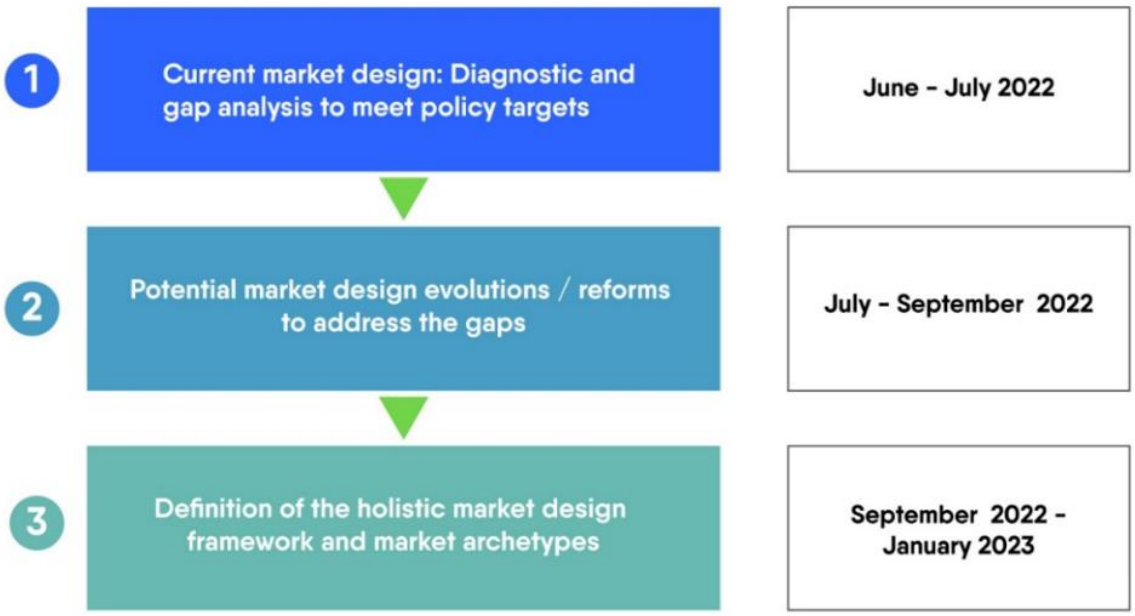
In November, the Electricity Association of Ireland launched our corporate strategy for 2022-2025 (event summary here), which focuses on the transition to a net zero energy system. At the Mansion House event Industry representatives discussed the challenges the sector faces in achieving this goal, and the impact on customers was paramount.

Speakers addressed the need for an electricity market that supports investment and a retail market that engages customers and supports them through transparency and accessibility. Eurelectric and Compass Lexecon addressed the same topics in their recently published Electricity Market Design Fit for Net Zero, what follows is a review of the retail measures proposed and the Irish context to the report produced. The study, which was partly funded by EAI, followed a structured and interactive approach in three phases outlined in the graph below.

What's Working?

The report notes that the current market design is not the root cause of the high electricity prices witnessed across Europe. A gas supply crisis was created due to embargos on Russian gas after the invasion of Ukraine. The subsequent policy interventions by the EU sought to tackle electricity prices through inframarginal caps.

Fig:
Approach to Market Design Flagship Study



Recommendations for Retail Sector cont.

The EU Commission also brought forward proposals on electricity market reform which are more of an 'evolution not revolution' approach. The Commission recognised that the current energy market design, based on marginal pricing, ensured efficient dispatch of generation and flexibility assets, reducing volatility despite exceptional circumstances in Europe.

ACER (in their recent review of the Electricity Market, available here) estimates benefit of €34b were achieved in 2021 due to a merit order approach and integrated markets.

'There is no better alternative to the marginal cost dispatch mechanism.

With growing decentralisation of renewables, preserving the current short-market functioning will be key to ensuring the efficient real-time dispatch of generation and flexibility assets and demand-side response, as well as efficient cross border exchanges of electricity.'

How does the wholesale market affect customer bills?

CRU in 2020 published a Factsheet which indicated that wholesale costs contribute to 38% of a customer's bills, within this energy costs including fuel costs, capacity and fixed costs of operating generators and market operator costs are included.

Similarly, Network Costs contribute to 31% of a customer's bill which incorporates the cost of transmission and distribution of electricity and gas as well as investment and maintenance of the network infrastructure.

While the current volatility in Gas prices and subsequent government intervention on VAT and a negative PSO have altered this breakdown, the fact remains that the operation of the wholesale market has a significant impact on customer bills – providing the greatest contribution to domestic electricity bills.

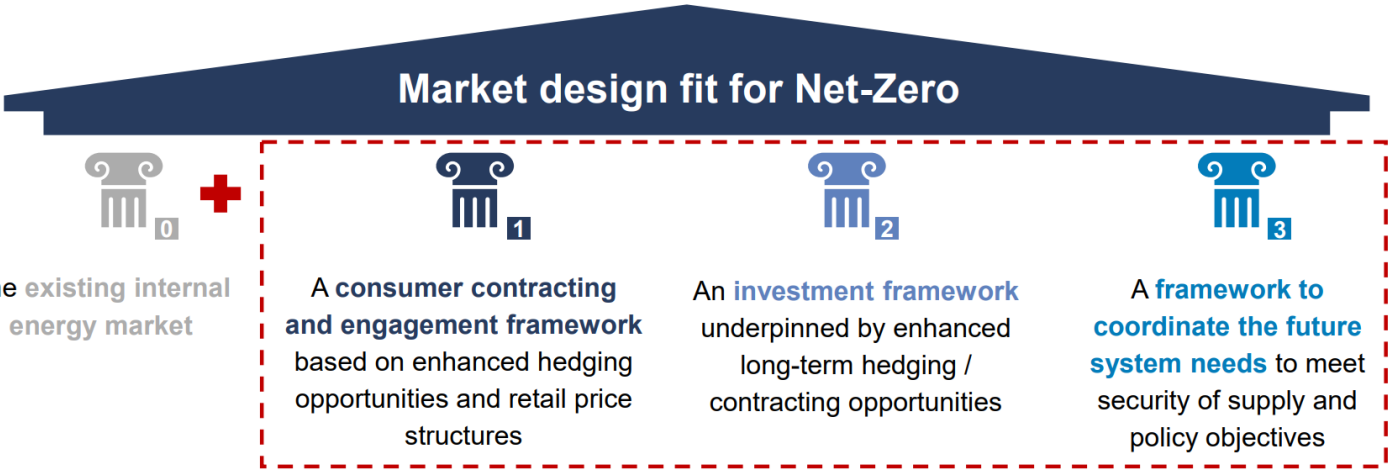
Savings accrued due to the efficient dispatch of low carbon generators and competition promoted through marginal pricing has a real impact and will be a key component in a net zero system.

Whilst the wholesale market is working, the study identified 3 key pillars that need to be implemented to further improve existing arrangements, identified in the chart below. These are positions that EAI strongly align with.

Customer Engagement in the Market

The system now needs to pass the benefits of cheap renewables onto the customer more directly. Electricity customers have historically been inactive in the market, made so through steady and affordable prices.

The goal of the Smart Metering Program is to facilitate the customers participation in managing their consumption, however, recent figures in Ireland from the CRU (April 2023) show that out of the 1.2 million smart meters installed, only 14% have accessed data services through ESBN and 7% have opted for time of use tariffs.



Recommendations for Retail Sector cont.

As retail prices began to increase to reflect geopolitics, customers proportionally became more aware of their consumption and are seeking methods to reduce bills. In order to reduce volatility in customer bills the Eurelectric report recommends that Customers should be able to avail of long term contracts with their suppliers and that barriers should be removed to facilitate this.

The report recommends introducing a consumer contracting and engagement framework adapted to different consumer segments: including elements which.

i) **Guarantee adequate information to consumers and sensibilisation of risks to long term commitments**. This could be achieved through strict implementation of Art. 10 of the Electricity Directive requiring suppliers to provide fair and transparent T&Cs in plain language to customers. A specific provision on informing customers of the risks of fixed/ long term contracts is also recommended.

ii) **Ensure supplier resilience to avoid consumers suddenly losing their suppliers.** Developing metrics/ tests on supplier hedging as well as stress tests for suppliers. **Foster hedging to protect consumers against medium to long term price volatility which requires consistent customer commitments.** Achieved through removing barriers to PPA's for smaller energy users, as well as enabling suppliers to hedge longer term through improved liquidity arrangements in the forward markets.

iii) **Empower customer through demand side responses.** Achieved through the full implementation of the Clean Energy Package and particularly the smart metering program. This would facilitate greater products on the market including time of use tariffs, dynamic pricing, critical peak pricing, and dynamic rebates.

Conclusion

The key takeaway for the Irish market is to ensure supplier resilience and to facilitate longer term commitments with customers through a variety of products, utilising the smart metering program. This will be facilitated by removing the current barriers to accessing customer usage data from smart meters.