EP UK Investments

A member of the EPH Group

CMC_04_24 – Recovery of Net Present Value Lost as a Result of No-Fault Delays to New Capacity

Capacity Market Workshop 36

Modification Background

- This modification seeks to amend the Capacity Payments for the first year of a contract which has received an extension to its Capacity Quantity End Date and Time under the Capacity Market Code.
- The purpose of this amendment is to recover costs incurred as a result of a No-Fault Delay for which the Regulatory Authorities issue an extension.
- EPUKI believes that this modification is consistent with the intended purpose of the extension modifications previously approved by the Regulatory Authorities in protecting New Capacity from delays which would threaten feasibility, in instances where the delay is not the fault of the Participant.
- Under the current rules, where a participant incurs a delay and a subsequent extension, there are two impacts on Net Present Value, (i) construction delays resulting in higher construction costs, and (ii) moving revenue to the end of the contract through the extension mechanism results in a lower NPV for the project.
- Under this proposed modification, a Participant who receives an extension could apply to the Regulatory Authorities for the recovery of these costs, collectively termed "*No Fault Delay Costs"*. EPUKI envisions an application process similar to that in place for the USPC, whereby projects would submit an application for NFDC recovery along with supporting evidence justifying the request.
- The approved NFDC would then be recovered by the Participant over the first twelve months of the capacity contract.

Modification Legal Drafting

- The drafting of this modification requires a Participant to have received an extension under one of the relevant provisions of the Capacity Market Code.
- This enables the applicant to make an application to the RAs for the recovery of No Fault Delay Costs as set out in the proposed modification (J.5.9.2 – J.5.9.4).
- Approved NFDC are then calculated on a per MW basis as the No Fault Delay Costs Payment under J.5.9.5.
- This payment is added to the current Capacity Payment Price for the first twelve months of the contract in a manner which is consistent with the RAs' indexation modification.

Justification for Modification

- The SEMC has previously acknowledged the termination risk that no-fault delays represent to New Capacity. While modifications have been introduced to address this (SEM-23-001 and SEM-23-101), projects which incur such delays are still exposed to NPV reduction through real cost increases and the cashflow impact of delayed Capacity Payments.
- This limits the effectiveness of extensions under J.5.6, J.5.7, and J.5.8, and means that a significant risk remains that developers will be unable to make an investment decision to deliver New Capacity projects due to reduced return on investment. This modification would address this risk.
- It is critical that New Capacity is added to the all-island system as demonstrated by the adequacy deficits identified in the Generation Capacity Statement for 2023 – 2032. The significant risk exposure faced by developers of New Capacity was illustrated through the outcome of the 2027/2028 T-4 Capacity Auction, where no new builds took contracts, and the cancellation of the 2027/2028 T-3 Capacity Auction.
- Consequences of not delivering New Capacity are significant. The Transmission Network Allowed Revenues Paper (CRU2023103) indicated that the CRU has already spent approximately €965m on emergency generation measures. EPUKI has calculated (based on technology de-rating and four-year asset life) that this equates to €2,477,032/MW/year which equates to fifteen times the current Auction Price Cap.
- EPUKI believe that this modification would deliver more transparency and efficiency for consumers by ensuring that New Capacity which is procured competitively can be delivered. This is aligned with the interest of consumers and Security of Supply, and consistent with the principles introduced through previously approved extension modifications.

Further Information – No Fault Delay Costs Examples

- The modification introduces a new variable: *No Fault Delay Costs*, which includes both real construction cost increases, and NPV reduction incurred through no-fault delays. EPUKI envisions these costs consisting of the following:

NPV Reduction	**Construction Cost Increases**
This represents the NPV reduction incurred by a project which incurs a delay and requires an extension. Assume a project contracted for October 2028 incurs a six-month delay due to a third-party planning appeal, and subsequently receives an extension under J.5.6. Six months of Capacity Payments will be moved from October 2028 to October 2038. From a cashflow perspective, Capacity Payments received in 2038 are worth considerably less than those at the beginning of the contract.	Construction cost increases could include the cost of retaining necessary crews on-site to complete works where there has been a delay. For example, if a gas or grid connection is delayed durign commissioning it would be necessary to keep crews on site.

Further Information – Worked Example

- Assuming a 300MW OCGT incurs a six-month delay to its start date as a result of a third-party planning challenge.
- Based on a discount rate of 9%, a CM price of €163,757 and a de-rating factor of 0.803, this would incur a nominal loss of €7.06m. Adjusting for real value, this would be €10m.
- We also assume €2m in additional construction costs, noting that these costs can vary on a project by-project basis. This gives a total No-Fault Delay Cost of €12m.
- If a unit applies to the Regulatory Authorities for recovery of this value, and it is approved, its No-Fault Delay Cost Payment will be calculated as follows:

$$\frac{€12{,}000{,}000}{240.9MW} = €49{,}813.2/MW$$

- This will mean that for the first twelve months following Substantial Completion, the projects Capacity Payment price will be €213,570.2/MW. This will enable a project to remain NPV-neutral even where it has incurred a no-fault delay.

Further Information – Process Outline