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Dear All

Transmission Constraint Licence Condition call for input and guidance consultation

The Flexible Generation Group (FGG) represents the owners of and investors in small scale, flexible generation and storage. These power stations are embedded in distribution networks and provide a variety of vital services to the system operator and the DNOs to help them deliver secure, economic supplies to electricity customers. We have assets connected to both TOs and DNOs and have been active in the Balancing Mechanism (BM) and ancillary services.

As a matter of principle FGG does not support the TCLC. If Ofgem believes a genco is abusing a dominant position it can use competition law. When looking at the fines Ofgem has levied, the analysis underlying their decisions is not public so it is impossible for parties to know what Ofgem believes is an 'excessive benefit'. It is also not acceptable that the ESO knows when there is a constraint and how it will impact the market, but it is not made to share that information with the result that generators are made to trade with less information than their counterparty; NGESO.

Ofgem notes the TCLC has been in place since 2012 but provides no compelling case that the competition law could not work instead, nor why it would need to extend the scope of TCLC to cover more parties than already covered. Further, what has been the cost of Ofgem's investigations to themselves and the impacted parties? Without some proper evaluation of the benefits of the TCLC there cannot be a case for retaining it, let alone extending it. Ofgem's default should be to enhance markets, improving how they work and not on increasing red tape.

While some FGG parties have a generation licence they do so because they are storage and not because they are licensable plant under the Electricity Act. Others have no licenses, but all believe that they are covered by competition law.

Market Information

It is not the fault of parties that there are so many constraints across the network. When looking to bid or offer into the market parties should be aiming to be the marginal plant, maximizing profits. If they do not know there is an active constraint then they cannot know that their pricing behaviour, rational in a competitive market, could be considered market abuse. Companies such as ours do not have the resources to monitor all the NGESO data, so believe ALL constraints on the TO and DNO networks should be published in real time.

Application of TCLC to other services

FGG members participate in a number of the ancillary services markets, some of which may be then used to manage constraints. However, Ofgem makes no case that these markets have been subject to any abuse of a dominant position. In fact, these markets appear to be very competitive, with most seeing falling prices. While Ofgem talks about schedule 7 trades, it seems to be keen to place additional regulation on a variety of parties.

As noted above, many ancillary services providers do not have generation licenses, so it is not clear how Ofgem would implement its proposals. It is not clear to us that Ofgem has any powers to force parties to be licensed. The proposals would therefore create two different levels of regulatory risks.

FGG has long argued that NGESO takes far too many actions ahead of time when there is often sufficient plant in the BM to meet their needs. Ofgem should, instead of focusing on increased regulation of genscos look at the skip rates seen in the BM. If NGESO used more flexible plant in real time then they would take less pre-gate closure actions. Alternatively, if a constraint is to be active for sometime, it could hold auctions for bids to help over longer periods.

TCLC on Offers

This proposal would see the death of storage. Highly flexible plants that are used to manage constraints would not be able to reasonably earn the income they need if they are having bids and offers effectively curtailed by Ofgem. The models that support investment in storage rely on being able to extract economic rent from their operations, not having their assets stopped from storing power at economic prices.

Again, Ofgem offers no evidence that there is an issue with competition with respect to offers in the BM. There is in fact a lot of competition and therefore any additional regulation would bring no benefit. And as noted above a party may not even know there is a constraint. Instead, they may have been expecting to import behind a constraint and then move to export, or to no change in state, depending on wider market prices. As already said, the market trades blind to many constraint periods.

Capping profits

If Ofgem and DESNZ want to move to regulate prices then it will kill all meaningful competition as the supply price cap has. How Ofgem would set these prices, which periods they apply to, etc. would be an extraordinary intervention and suggests Ofgem does not believe in markets at all.

Again, the impact on storage is likely to be far more detrimental than to other technologies. It seems to undermine the opportunities that the market should want storage to respond to. If Ofgem insists on undermining the business case for storage, then it will damage all of the investment momentum that the market has achieved.

General Pricing

While it is to be welcomed that Ofgem is consulting on its TCLC guidance, the regulation seems unfit for purpose. The issue remains that Ofgem has not clearly defined the way it judges 'excessive benefit', and the guidance suggests that it is actually asking parties to operate in a manner that requires parties do not operate as the rational economic agent that economic theory says they should and that the operation of a competitive market requires. The fact Ofgem's two inquiries took 2 years suggests that Ofgem also struggles to use the TCLC.

Ofgem suggests that "where a bid price is set solely with reference to the prices of other generators, without any assessment of the costs and benefits being bid down, that approach carries an intrinsic risk of breaching the TCLC." While some gencos must make a judgment about how much profit they need to export, and others need to worry about safe shut down, etc., generally in competitive markets players should be aiming to be the marginal plant, maximizing their profits.

The BM is a pay-as-bid market, which by its nature creates an incentive for plants to price their bids at the highest price they think will be accepted by reference to the prices of other BMUs, with the aim of being at the same level as the anticipated marginal bid. This is rational behaviour in a competitive pay-as-bid market, such as the BM and this is behaviour that suggests the BM is a functioning market, which Ofgem should welcome. Further, the genco does not know how long its bids will be accepted for.

Where parties are concerned that they could be in a dominant position in a market they need to be careful about not abusing that position. However, given the lack of market information very few gencos will know they are in such a position. If Ofgem seeks to suppress market prices, then it risks increasing the Capacity market or CfD costs as the gencos will need to make up money missing from the energy markets in other ways.

The time span that assets are profitable over can vary widely. A genco may run very infrequently, so needing to make more money when it is called or called off. Some gencos can have a very bad year or two and then will try to claw back to profitability when they can.

Parties will also have different views of their future income streams, or locked in different fuel prices, so making different decisions today than say last year. It is a widely acknowledged issue with capital intensive markets that they can be very cyclical, so parties may have very good years, followed by very bad ones. To investigate parties for what appears to be rational behaviour for limited periods therefore seems to just add to regulatory risks.

While defining 'excessive benefit' Ofgem seems to have lost sight of the fact that it is allowing NGESO to buy DFS for £3,000/MWh and above, far off any offer prices from gencos. These customers are not investigated for 'excessive pricing' and yet they are not consuming and we would assume their avoided costs are nowhere near this level. NGESO has also been allowed to call on coal plant, when far cheaper plant has been available in the market. Why are these actions alright?

It is unfortunate to see Ofgem putting so much effort into the micro-regulation of large gencos rather than focusing on trying to increase competition. There are so many ways Ofgem could increase competition rather than regulation, such as:

- Making the ESO and DNOs publish all constraints in real time so parties reasonably know if they are in a dominant position;
- Properly investigating and getting NGESO to stop the high skip rates being seen that leaves cheaper plant unused in the BM;
- Buying more ancillary services if they can be used to alleviate constraints more cheaply removing the arbitrary ESO position that 'ancillary services are just for system issues';
- Making the ESO use embedded assets to help manage TO constraints, which should be possible where there are GSPs that export or regions with storage that can import; and
- Ensuring that DFS, or other DSR, is not bought and dispatched in regions where it can make constraints worse.

If there is anything Ofgem would like to discuss further please do not hesitate to contact me.

Yours sincerely



pp Mark Draper
Chairman