Making a positive difference for energy consumers

Capacity Market Rules Change

Reference number*(to be completed by Ofgem)*: **P048**

Name of Organisation(s) / individual(s): UKDRA	**Date Submitted:** 23 January 2015
Type of Change: ☐ **Amendment** ☐ **Addition** x **Revoke** ☐ **Substitution**	**If applicable, whether you are aware of an alternative proposal already submitted which this proposal relates to:** Not aware of any alternative proposal

What the proposal relates to and if applicable, what current provision of Rules the proposal relates to *(please state provision number)***:**

The current rules prohibit DSR CMUs from participating in both the Transitional Arrangements and the main T-4 auction, that is, the TAs and the main T-4 auction are mutually exclusive, even though the delivery years for the TA precede the first delivery year for the T-4 auctions. If a CMU has secured an obligation via a T-4 auction, it cannot participate in the TA. This proposal would eliminate that exclusivity.

Description of the issue that the change proposal seeks to address:

This exclusivity between the Transitional Arrangements and the main T-4 auction has a number of unintended consequences which will increase costs to consumers and reduce competition in the energy market, and positions the policy for DSR at odds with the policy of other technologies.

Costs to consumers:
The existing exclusivity is detrimental to consumer interests in that it leads to increased cost to consumers (see answer to later analysis question) by reducing competition in the T-4 auction, since it means that less DSR will participate in those auctions than otherwise. Those T-4 auctions procure the vast majority of the capacity for each delivery period, and it is in these auctions that the market should seek to leverage the lowest cost options. For each £1/kW by which DSR reduces the main auction clearing price, consumers will save approximately £50m per annum. In contrast, reducing the T-1 auction clearing price by £1/kW will save only £1.5m. These implications relate directly to Ofgem's duties, particularly its primary duty to "*…protect the interests of…consumers*" and its requirement to do that "*…wherever appropriate by promoting effective competition…*"

Negative impacts on the DSR industry, which DECC has stated it wants to promote:
The current CM Rules require DSR to choose between short-term, year to year, provision of capacity, and having future revenue certainty which helps to make the case for new DSR. This

does not fit with the stated policy that the TAs should “encourage enterprise” in the DSR industry.

To achieve the purpose of the TA; i.e., to attract new DSR to the capacity market, the DSR industry needs near-term revenue opportunities - which the TA are designed to provide - AND long-term revenue certainty, which is currently not possible due to the exclusivity rule. By keeping the rule it is more difficult to attract new DSR. Removing the rule will help DSR and increase the competition in the T-4 auction at the same time. The current rules essentially inhibit the very purpose the TA were designed to promote, that is, help develop DSR for participation in the enduring market. Instead, the current rule places restrictions on that participation in the enduring market, negating the value of the investment in the TA for both the DSR industry and the consumer.

The current exclusivity rule forces an uncertainty onto the DSR industry that is unfair. DSR, if it elects to participate in the TA, can only enter the first two delivery years of the enduring market via the T-1 auctions. Although there is 1.25GW guaranteed to be required in the first T-1 auction, the new DSR that DECC is seeking to encourage is being forced to compete with assets that have also had the opportunity to participate in the T-4 auction.

<u>Proposed rule change is consistent with broader DECC policy:</u>

The current exclusivity rule, while seemingly supported by DECC, is actually inconsistent with stated DECC policy relating to development of new sources of capacity in general. By current DECC regulations, if a potential CM participant other than DSR were to be enjoying a subsidy (for example, low carbon support schemes), it could elect to participate in the T-4 so long as it committed to give up its subsidy *<u>in time for the start of the CM delivery period</u>*. See Regulations 15 and 16 that clarify this. So for other potential CM participants, the issue for eligibility is concurrence with the delivery period; for DSR the eligibility issue is sequential (i.e., the TAs occur before the first delivery period). Even if one were to accept the premise that the TAs were solely a subsidy for DSR, the resource should be able to participate in the subsidy up to the time of the first delivery period, so long as there were no overlap. That would be comparability with other resources and comparability with DECC broader policy. But by virtue of the exclusivity rule, DSR cannot equally participate. Thus DECC has built a biased subsidy into the CM-- one type of resource can utilize subsidies but another cannot. *This is <u>biased and unfair</u>.*

The discrepancy and discrimination between the T-4 and TA exclusivity for DSR vs the fact that other potential CM participants are not excluded from receiving incentives to grow their industry and make them more competitive, but are still be allowed to participate in the T-4 auctions from the start, is a critical barrier for DSR in the implementation of the enduring Capacity Market.

If applicable, please state the proposed revised drafting *(please highlight the change)***:**

Remove 11.3.2.b “any Non-CMRS Distribution CMU or DSR CMU that includes any Generating Unit or DSR CMU Component that forms part of a CMU that has been awarded a Capacity Agreement in a Capacity Auction(other than a Transitional Capacity Auction) in any previous year” in its entirety.

Analysis and evidence on the impact on industry and/or consumers including any risks to note when making the revision - including, any potential implications for industry codes:

The change should see a reduction in total consumer cost, based on analysis by NERA (available at http://www.nera.com/content/dam/nera/publications/2014/PUB_Anstey_DSR_0814.pdf) and should support the development of the UK demand response industry. We do not see any implications for industry codes.

Details of Proposer *(please include name, telephone number, email and organisation)*: UK Demand Response Association, Herb Healy; Tel: +1-860-306-4503; hhealy@enernoc.com