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1<sup>st</sup> May 2015

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## **Electricity Market Reform (EMR): Statutory consultation on changes to the Capacity Market Rules pursuant to Regulation 79 of the Capacity market Regulations 2014**

Dear Adam,

RWE welcomes the opportunity to respond to the Ofgem Statutory consultation on changes to the Capacity Market Rules pursuant to Regulation 79 of the Capacity market Regulations 2014 (the Consultation Document). We are responding on behalf of RWE companies operating in the UK.

We support changes that clarify and simplify the Rules. However, this latest set of changes must be reviewed in the context of the consultations undertaken by DECC (including for example the definition of new build and the inclusion of interconnectors in the rules). In this context:

- There are a complex set of pending revisions to the Rules that interact and potentially may overlap. It is difficult therefore to understand fully the implications of the latest set of changes in the Consultation Document without considering the effects of other changes;
- It would be helpful if Ofgem were to publish a baseline version of the Rules as soon as practicable. This would help us to comment fully on the changes identified in the Consultation Document;
- We are having some difficulty in tracking the relevant changes into the legal drafting of the Rules. Ofgem should develop a serviced electronic copy of the Rules (and Regulations). This would enable parties to monitor the evolution of the Rules.
- We are concerned about the rejection of certain proposals based on Ofgem assertions and without any discussion on the relative merits of the proposals (or any alternatives)

Our responses to the specific questions are included in Annex 1 to this document. If you have any comments or wish to discuss the contents of this letter then please do not hesitate to contact me.

Yours faithfully

*By email*

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## Annex 1: RWE Response to the Consultation Questions

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### Q1. CP06, CP25, CP34, CP41 and CP50: Qualifying Capital Expenditure for New Build

**CMU:** We invite stakeholders to provide us with information, and factors, backed up with evidence as far as possible, that we should take into account in considering: When should the Rules be amended to introduce the period for qualifying expenditure of 77 months prior to the start of the relevant delivery year?

The decision to include a specific date in the original capacity market rules was essentially arbitrary and designed to prevent any investment hiatus that could occur as a result of uncertainty surrounding the delivery of Government policy.

The principle associated with determining a “cut off date” for qualifying capital expenditure for a four-year ahead auction is an essential component in the capacity market rules. This date should be set in relation to the expected lead time associated with new build which underpinned the decision taken by DECC to hold an auction to take place four years ahead of the relevant delivery year.

In essence the “cut off date” relates to the time that it takes for parties to mobilise, construct and commission a new power station following planning consent. Therefore the lead time should be related to the period required to build a power station as defined by the capacity market lead time. In addition, given the principles that underpin the capacity market arrangements, the change should take effect as soon as possible and in advance of the 2014 auction (i.e. there should be no delay until 2017).

With regard to specific evidence on construction lead time we note that DECC have commissioned various reports on levelised cost assumptions for various technologies. For example in the Parsons Brinckerhoff Report commissioned by DECC in 2014<sup>1</sup>, the authors state the following for CCGTs:

*“Given a typical plant construction period of around 30 months this would suggest that around three such plants could be completed per year within this constraint, offering between nine and twelve gas turbines in combined cycle.”* (Section 2.7, Page 15)

In addition in the Parsons Brinckerhoff report the authors state the following in relation to OCGTs:

*“There is no recent UK experience of construction of large OCGT plants. However, having a much higher proportion of factory assembly, OCGT plants require substantially less construction work with each generator unit completed after about 12 months site work with typically one third of the effort required for a CCGT. Hence potentially between two and three times the number of OCGT generator units can be completed per year than CCGT generator units.”* (Section 2.7, Page 15)

Based on this work and other similar reports<sup>2</sup> commissioned by DECC there is considerable evidence that the lead time for the construction of new capacity is well understood and is significantly less than 77 months.

As we noted in our proposal for change to the Capacity Market Rules, the Rules could be amended to include the following evergreen definition of qualifying capital expenditure and associated lead time:

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<sup>1</sup> The report can be found at:

[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/315717/coal\\_and\\_gas\\_assumptions.PDF](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/315717/coal_and_gas_assumptions.PDF)

<sup>2</sup> See for example Parsons Brinckerhoff Electricity Generation Model: 2013 Update of Non-Renewable Technologies, at <https://www.gov.uk/government/publications/parsons-brinckerhoff-electricity-generation-model-2013-update-of-non-renewable-technologies>

*“with respect to a Prospective Generating CMU, the Capital Expenditure (excluding contingency) incurred, or expected in the reasonable opinion of the Applicant to be incurred (either by the Applicant or another person), between ~~1 May 2012~~ the commencement of the Calendar Year that immediately precedes the year in which the Prequalification Window commences and the commencement of the first Delivery Year to which the Application relates, divided by the De-rated Capacity of the Generating CMU that is expected in the reasonable opinion of the Applicant to result from such Capital Expenditure”*

As we noted in our proposal, this change can be justified against the Capacity Market Rules Change Objectives as stated in the “Change Process for the Capacity Market Rules – Guidance” published by Ofgem as it will:

- promote investment in capacity to ensure security of electricity supply by clarifying the Rules with respect to Qualifying Capital Expenditure and ensuring that the Rule operates on an enduring basis with respect to this definition;
- facilitate the efficient operation and administration of the Capacity Market by removing the need to address the fixed calendar date issue in the definition of Qualifying Capital Expenditure; and
- ensure compatibility of the Capacity Market Rules with other subordinate legislation under Part 2 of the Energy Act 2013.

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**Q2. CP01, CP07, CP25, CP34, CP41 and CP50 Qualifying Capital Expenditure for**

**Refurbishing CMU:** We invite stakeholders to provide us with information, and factors, backed up with evidence as far as possible, that we should take into account in considering: (i) Should the starting point for qualifying refurbishing expenditure be prequalification results day or auction results day? (ii) Should this new starting point apply from 2016?

We agree with Ofgem that a change in the rules is required with regard to Qualifying Expenditure for Refurbishing CMUs. Our preference for the commencement date is the Auction Results day, since this date confirms that the relevant CMUs has a capacity agreement and should be the basis for commencement of the expenditure. Such a change would, in relation to the Capacity Market Rules objectives:

- promote investment in capacity to ensure security of electricity supply by ensuring that the qualification for a 3-year agreement relates to the completion of a refurbishment of plant that occurs between the completion of the auction and the commencement of the delivery year, thereby enhancing security of supply by ensuring that additional capacity is being delivered;
- facilitate the efficient operation and administration of the Capacity Market by clarifying the arrangements that apply in relation to the qualification for 3-year agreements; and
- ensure compatibility of the Capacity Market Rules with other subordinate legislation under Part 2 of the Energy Act 2013.6

We do not understand Ofgem's reservations about implementation. The issue relates to the principle associated with the commitments made by parties with respect to refurbishment capital expenditure. In order to promote the efficiency of the Capacity Market Rules and ensure value for money for customers, we believe that such a change should be implemented as soon as practical, and should apply for the 2015 auctions. We can see no reason for any delay to this change.

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Q3. **CP69:** Do you have any views on whether and how the Rules should be amended to prevent applicants being able to provide a calculation of connection capacity close to the value of entry capacity in the manner described in CP69?

The Capacity Market Rules are clear in relation to the connection capacity and the de-rating methodology. We do not believe that there is a case to change the rules in this area. We have seen no evidence that supports National Grid's assertion that the application of the current rules create any issues associated with security of supply where there de-rated connection capacity is close to the transmission entry capacity. The issue of connection capacity and transmission entry capacity was well understood during the discussion on the development of the capacity market rules. It was agreed that connection entry capacity would be used as the basis for de-rating. It is up to market participants to manage efficiently their transmission entry capacity in relation to their obligations under Capacity Market Agreements.

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Q4. **CP74:** Do you agree that duration bid amendments should only be allowed to reduce during the auction?

We agree that duration bid amendments should only be allowed to reduce during the auction.

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Q5. **CP46:** Do you believe that DSR CMUs should be able to add, remove and reallocate CMUs? Please explain your answer. Do you think there are potential downside risks to this, as we describe above? If so, how would you suggest we mitigate these downside risks?

We believe that the issue of DSR resources that are capable of adding, removing or reallocating CMUs should be considered in greater detail. However, our starting point is that capacity market providers should make firm commitments to deliver the required capacity and there should be no possibility that components can be reallocated merely to achieve any relevant tests or to change configuration during delivery periods under system stress conditions.

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Q6. **CP24:** Do you have any reasons or evidence for why we should not also include OC.6.7 as a form of load reduction in the definition of Involuntary Load Reduction (in addition to our proposal to make the amendment suggested by CP24)?

We agree with the proposal to include OC.6.7 as a form of load reduction in the definition of involuntary load reduction.

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Q7. **CP49:** Do you have any evidence to show that CHP is failing to prequalify or that there would be benefits to allowing embedded generation to bid as a DSR component?

We have no evidence to show that CHP is failing to prequalify. We strongly support the role and potential for DSR within the capacity market and note that that DSR can be provided through embedded generation, displacement generation or load reduction. We therefore agree there would be benefits to ensuring that embedded generation can bid as a DSR component. For many DSR providers (or their contracted partners) DSR actions can provide a multitude of services and ensuring that all technologies are treated equally (irrespective of technology) will be critical to providing the policy framework required to support and encourage the greater use of and investment in all types of DSR assets.