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Ecotricity Response to Capacity Market: proposals to simplify and improve accessibility in future capacity auctions

Dear Energy & Security Team,

Ecotricity is an independent renewable energy generator and supplier, with around 190,000 gas and electricity customers. Our commitment to those customers is that the money they pay for their energy bills will contribute towards powering the UK by renewable sources. We have followed this pledge since first generating renewable electricity in 1998, and are now at the forefront of new renewable generation with ongoing research into tidal power, storage and biomethane.

We welcome this opportunity to respond to the consultation: the capacity market has a significant impact on us both as a supplier that pays into a levy for this, and as a potential entrant with storage. Over the past couple of years we have engaged with multiple consultations on its developments. We are also in the process of responding to the joint BEIS/Ofgem call for evidence on flexibility and their coal consultation.

The capacity market's current format, and this consultation's proposal to remove net metering, are in direct conflict with the Government's broader energy policy aims of: increased flexibility; the phase out of coal generation; and the decarbonisation of the energy market in an economically effective manner.

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These conflicting policies simply add costs to consumers and reduce the potential that the policies will be effective. We believe that the capacity market can and should be amended in a way that brings it in line with its other priorities.

In short our response argues that:

- The problem of double payments could be achieved through specifically removing capacity market participants from net demand calculations.
- The introduction of a carbon intensity limit of 450g/kWh would bring the capacity market in line with the Government's decarbonisation and coal phase out aim.
- Credit requirements should for DSR should not be increased.
- Proposals for increasing transparency should go ahead.

Net demand

We object to the proposal to amend the basis on which suppliers are charged from net demand to gross demand. Embedded generation reduces demand on the transmission network and, through a reduction in losses, is a more efficient means of producing energy. It is not clear why BEIS has changed their position on this and, whilst it has raised some legitimate concerns, we believe that there better ways of addressing these than the complete removal of net demand.

BEIS has stated that one of its motivations is a concern that some embedded generators could receive a benefit for reducing the relevant supplier's net demand and participate in the capacity market itself: essentially receiving a double benefit. We agree that this overcompensation should be prevented; however, we believe that it could be resolved by simply stating that generators who participate in the capacity market should not be counted as negative demand.

We are concerned that removing net demand entirely would negatively affect confidence in the solar and onshore wind markets, which have already suffered from significant cuts and political uncertainty. Although like other embedded benefits, the advantage from net demand is not necessarily considered bankable, it does make wind and solar more attractive sources of power for electricity suppliers. We would therefore urge BEIS to reconsider this proposal and at least wait until there has been a chance for the onshore wind and solar markets to recover before removing this advantage from them.

With the exception of concerns over double payments, it appears that this proposal has not been justified on objective analysis of whether embedded generation has been over-compensated for the system benefits that it brings. Rather, the real motivation appears to be concern over the high number of diesel generators that have secured capacity market contracts. We share the Government's concern that such highly polluting generation should not be receiving public funds; however, we believe that the approach taken is insufficiently targeted. There is no guarantee that it will reduce diesel's participation and, as noted above, it will have unintended consequences for other generators.

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A Carbon Intensity Limit for the Capacity Market

Rather than targeting all embedded generation, we believe that a far better approach to tackling diesels' competitive advantage would be to add a carbon intensity limit of 450g/kWh to the eligibility requirements for the capacity market. This is the level at which new large scale generators are required to reach under the Emission Performance Standards and therefore it would bring the Capacity Market in line with the Government's decarbonisation objectives.[1] By being below the level of unabated coal, it would also be in line with the Government's objective of phasing this out.

We are aware that the Government is committed to maintaining the position that the capacity market is technology neutral. By setting a specific carbon emissions limit, rather than targeting a specific technology, technology neutrality would not be compromised any more than any other eligibility requirements. Just as it is reasonable to require dispatchability, in order not to compromise availability under the capacity market; so too is it reasonable to have carbon limits to prevent the capacity market from conflicting with other policy priorities.

We would like to bring the Government's attention to a capacity market rule modification proposal that we submitted in November this year and enclose a copy for your information. Whilst we will continue to advocate this as a rule change, we believe that it would be strengthened via an amendment to the underlying Regulations[2] rather than simply amending the rules.

Credit Increase for Demand Side Response

We object to the proposal to increase the credit requirements for Demand Side Response (DSR) from £5k/MW to £10/MW. DSR has to date only formed a small part of successful Capacity Market Units and, whilst the most recent auction showed some improvement on this, at just 2.69%[3] of the total successful capacity, it remains a small player. It is important to note that the DSR market is dominated by smaller companies, who are less likely to be able to obtain a credit rating or letter of credit. This makes high credit requirements a more significant barrier to entry than is the case with larger players. In addition, as DSR tends to be made up of multiple small units, the impact of a failure of any individual unit does not have the same security of supply implications as the failure of a single large scale generator.

DSR is a key part of the BEIS/Ofgem flexibility proposals and therefore it would appear inconsistent to increase barriers to entry at a time when the Government wishes to increase its use.

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[1] For more information on this please see Aldridge J (2015) Mad maths: How new diesel generators are securing excessive returns at billpayers' expense, IPPR. http://www.ippr.org/publications/mad-maths-how-new-diesel-generators-are-securing-excessive-returns-at-billpayers-expense

[2] Electricity Capacity Regulations 2014 (S.I. 2014/2043) http://www.legislation.gov.uk/uksi/2014/2043/contents/made

[3] National Grid (2016) *Final Auction Results: T-4 Capacity Market Auction for 2020/21* https://www.emrdeliverybody.com/Capacity%20Markets%20Document%20Library/Final%20Results%20Report%20-%20T-4%202016.pdf (accessed 23rd December 2016).

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Rather than change the credit requirements for DSR at this point, we would suggest that BEIS keep a watching brief on DSR deployment both within the capacity market and more broadly. Any increase in credit requirements should only be made after there has been a significant increase in DSR participation.

Transparency

We support the proposed amendments to the transparency requirements with respect to State Aid. We agree that it is appropriate for payments from secondary trading, over delivery payments and under delivery penalties to be included in calculations of total state aid received. We believe that requiring the Electricity Settlements Company to publish 6 monthly reports on the cumulative amount of state aid received by all Capacity Market beneficiaries that receive over €500,000 is a sensible amendment.

Conclusion

We support the Government's aims of preventing double payment of Capacity Market participants that also receive the benefit from reducing net demand and the goal of tackling the competitive advantage that diesel generators has had. However, we believe that both of these goals could be better achieved through a more targeted approach. The former through excluding embedded generators that participate in the capacity market from net demand calculations and the latter through the introduction of a carbon intensity limit.

We are concerned that the proposal for increasing the credit requirements for DSR is unnecessary and ill timed. The limited success of DSR to date suggests that more needs to be done to encourage its participation in the Capacity Market and elsewhere. Doubling credit requirements would have the opposite effect.

We welcome the Government's proposals to increase transparency with respect to State Aid and ensure that all types of payments and penalties are included in this.

Ecotricity welcomes the opportunity to respond and hope you take our comments on board. We also welcome any further contact in response to this submission. Please contact Holly Tomlinson on 01453 769366 or holly.tomlinson@ecotricity.co.uk.

Yours sincerely,

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