



Open letter on the Five Year Review of the Capacity Market Rules and NGET's Incentives

ADE Response

Introduction

The ADE welcomes the opportunity to respond to Ofgem's open letter on the Five Year Review of the Capacity Market Rules and NGET's incentives.

The ADE is the UK's leading decentralised energy advocate, focused on creating a more cost effective, efficient and user-orientated energy system. The ADE has over 120 members active across a range of technologies, and they include both the providers and the users of energy. Our members have particular expertise in combined heat and power, district heating networks and demand side energy services, including demand response (DSR) and storage.

A more efficient rule change process

The Capacity Market is increasingly becoming too large for the current institutional arrangements to be sustainable. Last year, Ofgem received over 100 rule change proposals for a process with relatively limited time to review, decide on and then implement changes. It is also increasingly clear that there is very little legislative time in which to make associated changes to the Regulations where required.

Two examples illustrate the difficulties of the current process.

Firstly, introducing the ability to allocate and re-allocate components into CMUs is a crucial step in creating more of a level-playing field between generation and demand response. This issue was first raised in around 2014. Whilst acknowledging its merit, Ofgem and the Delivery Body have not been able to implement it – largely because it was a significant change for which the implementation would have taken significantly longer than the time available to the Delivery Body between Ofgem's formal decision on the rules and the start of the pre-qualification period. Ofgem have now taken the decision to implement component allocation through Of12 over an 18-month period in time for next year's prequalification.

Secondly, a number of modifications were raised in this year's change process to clarify the participation of non-exporting CHP. As with component allocation, Ofgem accepted that this was a flaw in the current framework that was discouraging eligible capacity from participation. However, they were not able to make the relatively simple changes required to the rules because it could have created a conflict with the definition of a non-CMRS unit within the Regulations and it was not possible, in turn, to make the small amendment to the Regulations needed to resolve this.

Through our response to BEIS' Call for Evidence for the 5-year review, the ADE has asked Government to revise the Regulations so that they concern the high-level policy intent but leave the detailed conditions to the Rules.

This change will help the Capacity Market to evolve more easily but by itself will increase the burden on Ofgem. Therefore, this could be done in parallel with a governance framework for the Capacity Market Rules that is more similar to the current Code Governance framework. This should involve a greater level of industry-led coordination and development with Ofgem retaining final approval.

If this is undertaken, there are a number of considerations that would need to be taken into account when establishing a more industry-led governance process.

Broader industry governance is currently facing a number of new difficulties as the energy system changes dramatically. This includes eligibility to propose changes, the difficulty felt across the industry in resourcing working groups over a number of months, the ability to access quantitative analysis where this is needed and the principle of representation versus independent expertise. These are difficult issues that are broader than reform of Capacity Market governance. However, it is important that if the rule change process moves in this direction, this new governance approach takes into consideration these current difficulties and tries to avoid replicating them in the Capacity Market.

In addition, a key benefit of such a new approach could be that changes can be developed at a different pace depending on their complexity – rather than being restricted to the very short timescales before the next delivery year as currently. If this is implemented, it would be important that there is good information on how changes are progressing and in which delivery year changes are likely to be implemented.

Secondary trading

Secondary trading is only beginning to be used within the Capacity Market but there are a number of changes that could support this further.

Regarding its administration, we do not consider that the current process of recording contact details for secondary trading is working effectively. Developing a central platform for identifying potential trading parties, for example within the Capacity Market register, may better facilitate secondary trading.

We consider that a number of changes could be made regarding the Rules and Regulations. Firstly, BEIS and Ofgem could allow traded capacity obligations to be met by a different CMU generation type, on condition the same de-rated capacity is met. Secondly, the interactions between SPDs and secondary trading should also be reviewed – in particular, allowing participants to transfer SPD testing requirements when trading obligations for less than the entire delivery year. Further, greater automation of the process should be explored with a view to reducing the current notice period for trading of five days. Finally, BEIS and Ofgem should also review whether the Capacity Minimum Threshold should be attached to the transferee rather than, as at present, the transferred obligation.

Further to this, the ADE has also proposed to BEIS through their 5-year review that the minimum threshold of 2MW is reduced. If this change is implemented, we would ask that

Ofgem make the associated changes to the Rules, including those regarding secondary trading to allow for smaller trades.

Simplifying the rules

The ADE agrees with Ofgem's view that the current complexity of the Rules places a significant burden on participants and should be reduced where possible.

Through the ADE's response to BEIS' call for evidence, we have asked Government to amend the definition of a "non-CRMS distribution CMU" as "a generating unit which exports electricity to a distribution network..." to "a generating unit which exports electricity to a Distribution Network or on-site consumer and is connected to a Distribution Network that is not a CRMS Distribution CMU"¹. If BEIS agree to this proposal, we would ask Ofgem to make the necessary rule changes to implement this for the next delivery year; as previously set out in proposed rule change CP261.

During the 2017-18 rule change process, CP246 was raised regarding how the definition of Relevant Balancing Services within Schedule 4 accounts for how Capacity Market and STOR sites interact. This was rejected on the basis that it required the implementation of P354 and ABSVD C16. As both of those changes will be in place by the next delivery year, we ask that Ofgem uses this 5-year review of the Rules to implement this rule change. We also note that through the ADE's response to BEIS' 5-year review, we have asked that barriers are removed to stacking system services with Capacity Market contracts. As the ESO's System Needs and Product Strategy progresses and TERRE is implemented next year, it is important that the Regulations and Rules support stacking across all appropriate services, including new ones.

NGET's incentives

National Grid's Capacity Market portal is at present quite difficult to use for participants. The ADE considers that there is merit in Ofgem and the Delivery Body exploring improvements that could be made to make the IT and pre-qualification process more intuitive and reduces the risk of participants making unnecessary errors.

We would also ask that BEIS, Ofgem and the Delivery Body explore the introduction of a rolling pre-qualification window – rather than the current 8-week window during Summer. This would evidently need to be reviewed alongside broader changes to the change process and overall scheme governance. If this is done, DSR tests should also be allowed to be carried out during the pre-qualification window before the Capacity Market auction. Finally, we would note that the ADE's has asked BEIS through their 5-year review to reinstate the full derogation to the Delivery Body to allow them to work with participants to correct errors.

For further information please contact:

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¹ As per CP261 proposed by E.ON