



Mark Copley  
Associate Partner, Wholesale Markets  
Ofgem  
5 May 2017

Dear Mr Copley,

**Re: Ofgem's statutory consultation on changes to the Capacity Market Rules 2014**

Green Frog Power builds gas-fuelled power stations utilising reciprocating engines. Efficient and flexible, our plant is exactly what the market needs. We have built more capacity that is reliable than any other British company in the past five years. We have 430MW of plant in operation and a construction pipeline exceeding 600MW. The entire fleet can start from cold in less than two minutes.

We welcome the opportunity to respond to Ofgem's consultation on changes to the Capacity Market Rules.

The process for rule changes is time consuming and complicated. Splitting and staggering the responsibilities between BEIS and Ofgem is ineffectual. It is becoming increasingly difficult to keep track of proposed and implemented changes. The Rules are becoming more complicated and prescriptive, rather than less, as intended. And it is ever more difficult to manage projects and

resources when actual final Rules are known at such a late date, in terms of prequalification.

We propose that BEIS and Ofgem adopt a joint approach to consultations and that this process starts earlier in the year. Industry would appreciate having only one consultation response to worry about (and we think BEIS and Ofgem would too), and one set of potential Rules changes to take into consideration while planning.

In terms of the proposed Rules changes in this consultation, we take issue with only one: the connection capacity proposal from Ofgem (Of15). We anticipate numerous issues with the proposed approach as outlined in the appendix to this letter. Primarily, we do not believe that the proposal will meet Ofgem's regulated CM Rules Objectives, particularly regarding the facilitation of the efficient operation and administration of the CM.

Yours sincerely,

Graz Macdonald  
*Head of Regulatory and Policy Analysis*  
*Green Frog Power Limited*

## Appendix

Green Frog Power have several thoughts and comments about Ofgem proposed Rule change OF15 - Calculating Connection Capacity.

- We approve of the idea of permitting CM participants to nominate their own connection capacity
- We do not agree with testing satisfactory performance to full capacity
- We strongly disagree with the imposition of a fine for failure to meet satisfactory performance requirements

Ofgem proposes to allow for generators to nominate their connection capacity because the current Rules are considered overly complicated (on this we agree) and can lead to potential overstatement of the capacity available to deliver in a system stress event.

Parties should be able to nominate their own connection capacity subject to a cap of TEC/CEC or distribution connection capacity. They should be able to demonstrate that they are able to meet the derated level against which they are paid and against which system security of supply is measured. It would greatly simplify the CM Rules to permit a less prescriptive approach to nominating full capacity.

We do not agree that this approach will cause parties to overstate their capacity in any material way. Parties will be incentivised to submit the highest capacity they are confident that they will be able to deliver in a stress event.

They will also want to ensure that they are able to meet the annual testing requirements.

It seems a stretch that parties would feel confident enough to withhold capacity in the hopes of keeping the CM auction price artificially high. There are dozens of entirely separate entities participating in the auction – far too many to make this a profitable strategy.

While possible that the cap (of TEC/CEC etc.) does sometimes overstate actual capacity – it seems that this amount is negligible when compared against the costs of trying to eliminate the risk entirely. Ofgem suggest that the overstated value is potentially in the range of 1-1.5GW across the whole system. This estimate must be on the very high side and the actual must surely be negligible for any given plant.

It is not clear that there is material impact on security of supply, since security of supply is measured against derated capacity and delivered derated capacity is vigorously tested against in advance of prequalification and during the Delivery Year. It is also the capacity against which the CMU is paid.

This issue only arises in the case of (probably older) existing plant, where the CEC is potentially outdated and there have been modifications of the capacity through time. We note that a plant's physical output can never exceed CEC or TEC, so this is a one-way risk for these plant.

The current rules require that all plant demonstrate their ability to reach the capacity they are paid for. While possible that, in some rare circumstances the derated level is the feasible maximum of their total capacity, we struggle to

believe that this is such a serious issue that warrants Ofgem's testing and penalty proposals, which we believe changes the fundamental fabric of the CM.

It is difficult to understand how Ofgem believes that this has a material impact on the functioning of the CM, particularly in the context of Ofgem's regulated CM Rules Objective to facilitate the efficient operation and administration of the CM.

We are very concerned about the implications of the proposed requirements for reaching full capacity for demonstrating historical generation and within Delivery Year satisfactory performance. The proposed imposition of a fine (£35/kW!!) for any under delivery changes the entire risk profile of the CM and undermines BEIS's policy intent regarding risk and investability.

It is clear to us that if Capacity is to be tested prior to prequalification and during the delivery year to full capacity, then capacity should be paid to their full delivered capacity. It would also require that the methodology for determining security of supply and the amount of capacity to procure must also change to reflect what is inherently a fundamentally different CM design in terms of reliability and targeted LOLE and security of supply.

This begs the question of how to implement the proposed new CM design while keeping the system stable as it interacts with the current design. It would not be possible to impose these requirements on plant that have existing CM agreements. Penalties are firmly protected in the Regulations (or at least there was a clearly stated intention to do so – it is possible that the legislation is not written well enough to provide the intended protections). To renege on the

promise given at the time of the introduction of the CM, that the fundamental penalty/reward risk profile of CMUs that had won Agreements would remain grandfathered, would have far reaching implications for regulatory reliability and investability.

Implementing this proposal means that there will be two tranches of plant with two sets of risk profiles in the same market. Plant with existing agreements under a different penalty and reward profile from new plant with new agreements undermines the potential for a secondary trading market.

How can one trade over delivery if derated capacity is no longer relevant? How can one buy coverage if one does not know definitively what its full CM income for the year shall be? Will System Stress penalties be paid back to the CMU if an agreement is subsequently reduced?

It is easy to think of plausible scenarios where testing to full capacity results in problematic and unintended outcomes. For example, imagine a CCGT has a serious outage in late October lasting through to February. Under current rules it would trade its obligation for the months it is out of commission to offset the risk of system stress event penalties. It would then meet its satisfactory performance requirements in February, March or April.

Presently, the CCGT only needs to demonstrate capability to its derated level. But what if the weather is warm that spring? What if this CCGT is unable to achieve its full capacity due to ambient temperature effects on efficiency?

Under the proposed rules, this CCGT would be fined for shortfall if unable to achieve 97% of its full capacity – entirely plausible under certain ambient

conditions. But they would then have a large fine and have their Agreement reduced to the achieved capacity, presumable retroactively. *Even though this plant had met its obligation as required to meet the current system security standards and even though it had purchased covering plant to meet any stress events and even though the plant is only paid for its derated capacity.* How does Ofgem imagine that these plant shall be able to manage this risk effectively or efficiently?

And what if this plant has a multi-year agreement? We presume it must have a chance to redeem itself in the following year. Or what if the plant has successive one-year Agreements? Will its future agreements be reduced too? Will the exorbitant fine apply to future years also?

There are many issues with Ofgem's proposed solution for connection capacity. We think that it would be simplest and most efficient to:

- Permit plant to nominate their connection capacity as they wish (with a cap of TEC/CEC etc.)
- Test and be paid to derated levels of capacity (as now)
- Remove the proposed penalty clause entirely

Withholding capacity in the implausible hope of altering the auction outcome or increasing provision of secondary trading (a good thing surely) seems unlikely in any material way. And similarly, materially relevant overstating of capacity is improbable, considering the risk of being unable to achieve the satisfactory performance requirements or paying system stress event penalties.