Executive Summary

The purpose of the Capacity Market (CM) is to ensure security of electricity supply by providing all forms of capacity capable of contributing to security of supply with the right incentives to be on the system and to deliver electricity when needed. The CM secures the capacity required to meet peak demand in a range of scenarios through auctions held four-years (T-4) and one-year (T-1) ahead of delivery.

This Government Response summarises the comments submitted by respondents to the following three CM consultations, and describes the Government's consideration of these comments in reaching its intended final policy position:

1. Consultation on future improvements[1] which ran between 03 February and 02 March 2020;

2. Consultation on carbon dioxide emission limits[2] which ran between 22 July 2019 and 13 September 2019; and

3. Consultation on proposed easements in response to the coronavirus (Covid-19) pandemic[3] which ran between 24 to 30 April 2020.

Consultation on Future Improvements

On 15 November 2018, a judgment of the General Court of the CJEU (Court of Justice of the European Union) annulled the European Commission's original 2014 State aid approval of GB's CM. This prompted the European Commission to carry out a renewed investigation of the scheme under State aid rules. The European Commission's decision, of 24 October 2019, again granted State aid approval to the CM ("the State aid decision"). The State aid decision notes that the Government has committed to implementing a number of improvements to the design of the CM to reflect recent market and regulatory developments, including those identified through our recent five year review of the effectiveness of the CM ("the Five-year Review").[3]

The Government ran a consultation, from 03 February 2020 to 02 March 2020 (the "Future Improvements Consultation"), seeking views on proposals to implement five of the six commitments referenced in the State aid decision, as well as a review of the exclusion from the CM of plants with long-term contracts for providing Short Term Operating Reserve (LT STOR) and other minor improvements.

In total, 33 responses were received from a range of stakeholders, including trade associations, and Capacity Providers. The proposals were widely supported by the respondents to the consultation with the exception of the proposal to remove the exclusion of LT STOR holders from competing in the CM. We nevertheless intend to remove the exclusion because there is no longer a sufficient risk of windfall profits. We can, therefore, confirm that the Government will proceed with most of the changes as proposed, with a few refinements in

[1] https://www.gov.uk/government/consultations/capacity-market-proposals-for-future-improvements
[2] https://www.gov.uk/government/consultations/capacity-market-carbon-dioxide-emissions-limits
[3] https://www.gov.uk/government/publications/capacity-market-5-year-review-2014-to-2019

the light of consultation. A full response is in Section A of this document. In summary, we intend to:

- Allow Demand Side Response (DSR) to apply to prequalify to bid for all the agreement lengths available in the CM (up to fifteen years) if they can demonstrate they meet the relevant capital expenditure (CAPEX) thresholds. This is in line with the original proposals in the consultation, with some minor refinements to reflect feedback from respondents.
- Reduce the Minimum Capacity Threshold from 2MW to 1MW and enable Secondary Trading of Capacity Obligations under the Minimum Capacity Threshold if an entire Capacity Obligation is being traded. For a partial trade of a Capacity Obligation, the Minimum Capacity Threshold will still apply. We have made no changes to our original proposals.
- Provide legislative underpinning for the long-standing 50% set-aside commitment for T-1 auctions and the methodology for determining the minimum amount of set-aside. This formalises that commitment and methodology as part of the auction parameter setting process for all capacity auctions going forward. We have made no changes to our consultation proposals.
- Introduce a formal, annual review of new capacity technologies not currently competing in the CM but which could effectively contribute to security of supply. We have made no changes to our original proposals.
- Introduce a reporting and verification mechanism for the introduction of CO2 emission limits in the CM in line with original proposals in the consultation, with some technical changes to address feedback from respondents.
- Remove the exclusion on LT STOR contract holders competing in the CM, in line with our original proposal.
- The minimisation of fraud and error in the CM remains a priority to the Government. However, we will not be implementing these proposals at this time, as we intend to wait until we have carried out further investigation and stakeholder engagement. We will consider fraud and error again in due course and, if necessary, will consult on updated proposals.
- Make two minor corrections to the Capacity Market Rules 2014 (“the Rules”), as per our original proposals.

Consultation on Carbon dioxide emission limits

Regulation (EU) 2019/943 of the European Parliament and of the Council of 5 June 2019 on the internal market for electricity (the recast “Electricity Regulation”), which came into force on 4 July 2019,[4] as part of the EU’s Clean Energy Package[5] includes a requirement for capacity mechanisms to apply carbon emission limits.

[4] https://eur-lex.europa.eu/eli/reg/2019/943/oj
[5] https://ec.europa.eu/energy/en/topics/energy-strategy-and-energy-union/clean-energy-all-europeans

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SECTION A: Government Response to the Consultation on Future Improvements

A.1 Introduction

On 15 November 2018, a judgment of the General Court of the CJEU (Court of Justice of the European Union) annulled the European Commission's original State aid approval of GB's CM, on the grounds that the Commission should have carried out a second stage investigation into the scheme before approving it ("the General Court Judgment"). The General Court judgment put the CM in a standstill period whilst the Commission carried out a second stage investigation. During the standstill period, the Government was unable to make Capacity Payments or grant Capacity Agreements conferring a right to receive Capacity Payments.[6]

On 24 October 2019, the Commission concluded its investigation and found that the CM, as operated since 2014, including during the Commission's investigation, complies with European Union (EU) State aid rules. The Commission's Decision of 24 October 2019[7] ("the State aid Decision") brought the standstill period to an end.

The State aid decision noted that the United Kingdom (UK) Government had committed to implementing a number of improvements to the CM's design to reflect recent market and regulatory developments, including several identified through a recent five-year-review of the effectiveness of the CM[8] ("the Five-year Review"). Implementation of these commitments is intended to ensure the continued compatibility of the CM with State aid rules in the future.

The Government ran a consultation from 03 February to 02 March 2020 (the "Future Improvements Consultation") which sought views on proposals to implement five of the six commitments referenced in the State aid Decision, as well as a review of the exclusion from the CM of capacity with long-term contracts for Short Term Operating Reserve (LT STOR) and other minor improvements.

It remains our intention to publish a separate call for evidence to gather views on the sixth commitment described in the State aid decision, on cross-border participation, as well as a number of priority areas for improvement identified in our Five-year Review. However, this work has been temporarily delayed to enable both the Government and industry to focus on dealing with the effects of the coronavirus pandemic.

The Government acknowledges that respondents raised several issues that were not covered by the consultation. We have not covered these in this Government Response as they are not relevant to the proposals and most were identified previously through the Five-year Review. We will take these into account as we continue to monitor the operation of the CM and will consider whether there is potential to address other issues through future amendments.

[6] https://www.parliament.uk/business/publications/written-questions-answers-statements/written-statement/Commons/2018-12-06/HCWS1154/
[7] https://ec.europa.eu/commission/presscorner/detail/en/ip_19_6152
[8] https://www.gov.uk/government/publications/capacity-market-5-year-review-2014-to-2019

A.1.1 Summary of consultation proposals

In the Future Improvements Consultation, the Government proposed to:

- Allow all types of capacity (excluding interconnectors) to apply to prequalify to bid for all the agreement lengths available in the CM (up to fifteen years) if they can demonstrate they meet the relevant capital expenditure (CAPEX) thresholds.

- Reduce the Minimum Capacity Threshold to participate in the CM from 2MW to 1MW.

- Enshrine in legislation both our commitment to procuring at least 50% of the capacity set-aside for the T-1 auction, and the existing methodology for determining the minimum amount of capacity to be set aside.

- Ensure the incorporation into the CM of any new types of capacity which can effectively contribute to addressing the generation adequacy problem, as soon as such capacity has the potential to contribute to addressing the generation adequacy problem.

- Establish a reporting and verification mechanism for the carbon emission limits to be applied to the CM.

- Remove the exclusion of capacity with LT STOR contracts.

- Add additional information items to the Capacity Market Registers to help reduce the risk of fraud and error.

- Make a few minor corrections and clarifications to the Capacity Market Rules 2014 (“the Rules).

A.1.2 Summary of responses to the consultation

In total, 33 responses were received from a range of stakeholders, including Capacity Providers, system operators and trade associations. The proposals were broadly supported by the respondents to the consultation. Specifically:

- The majority of stakeholders were in favour of allowing Demand Side Response (DSR) to access multi-year agreements and supported our proposals for facilitating this, as well as our proposals for mitigating the unintended consequences that may arise (in particular, the potential for an increase in battery storage to build behind the meter). We therefore intend to make changes to the Electricity Capacity Regulations 2014 (“the Regulations) and the Rules to allow DSR to access multi-year agreements in line with the original proposals in the consultation, with some minor refinements to reflect feedback from respondents. We have kept the framework for DSR access to multi-year agreements as similar to generation as possible, with some differences where necessary due to the nature of DSR compared to generation.

- The reduction in the Minimum Capacity Threshold from 2MW to 1MW was generally supported by respondents and considered to have limited impact on future capacity auctions by most respondents, who noted that smaller units could already enter the CM through aggregation. Several respondents did, however, feel that auction liquidity could increase, with a potential reduction in the clearing price, as more units, particularly DSR, could compete. We intend to implement changes in line with our consultation proposals.

- Respondents were generally in favour of providing a legislative underpinning for the 50% set-aside commitment and the 95% confidence interval methodology and were not aware of any associated unintended consequences. The 50% set aside commitment was considered by several respondents as a key enabler for technologies which did not view the T-4 as commercially viable. There was recognition amongst responses of the Government's commitment to introduce the change as described in the State aid Decision. However, several respondents felt the Government should retain the maximum flexibility possible in setting the capacity targets for CM auctions; with some citing concerns the proposals risked over procurement in T-1 auctions, increasing costs to consumers. We have made no changes to our consultation proposals.

- The majority of respondents were in favour of the proposal to introduce an annual review of new capacity types not currently competing in the CM. Respondents did not identify any capacity technologies unable to enter the CM, although hydro plants (tidal, wave, and ocean current) were noted by respondents as having potential to enter in future. Respondents in favour felt the proposal was appropriate and would meet the desired outcome. We have made no changes to our consultation proposals.

- The majority of responses expressed support for the approach proposed for the overall reporting and verification mechanism for carbon emission limits. Respondents also highlighted certain aspects of the proposals which could lead to unintended consequences or warrant fine-tuning. Aspects highlighted included a concern with the timescales available for all declarations to be submitted and verified ahead of the upcoming Prequalification period as well as a perceived unfairness of the formula for the calculation of emissions for some Combined Heat and Power (CHP) CMUs. We, therefore, intend to introduce a reporting and verification mechanism in line with original proposals in the consultation, with some technical changes to address feedback from respondents.

- The proposal to remove the exclusion on LT STOR contract holders from competing in the CM was opposed by the majority of respondents, several of whom citied their belief that these contract holders had made a business decision to opt for LT STOR over the CM. Concerns around market distortions and the potential for LT STOR revenues to increase were also raised. Those respondents in favour of revoking the exclusion noted that changes to LT STOR markets had lowered potential revenues from the contracts and that these are now similar to revenues from other balancing service contracts, whilst another highlighted the effect of the change would be small as so few Capacity Providers held LT STOR contracts. We intend to remove the exclusion as proposed in the consultation.

- Responses to the proposals on Fraud and Error were split. The most common reason given for disagreeing with this proposal was the increased administrative burden it would place on Capacity Providers to submit and then keep up to date, the name and

A.2 Agreement lengths for DSR

A.2.1 Impacts and the Capital Expenditure Thresholds

Consultation question 1:

We would welcome your views on the impacts that access to multi-year agreements might have on Unproven DSR participation in the capacity auctions, including on levels of participation and bidding behaviour.[9]

Consultation question 2:

Is the proposed application of the CAPEX thresholds for Unproven DSR fit for purpose? In particular:

(i) The definition of CAPEX for Unproven DSR

(ii) The application of thresholds at CMU level

(iii) The 77-month cut-off date. Should we reduce the cut-off date for DSR seeking to access multi-year agreements?

A.2.1.1 Summary of responses

21 and 23 respondents provided responses to Questions 1 and 2, respectively.

A.2.1.1.1 Allowing DSR to access multi-year agreements

The majority of respondents thought it was important that Unproven DSR be allowed to access the same multi-year agreements as Prospective Generating CMUs, to ensure a level playing field. A majority of respondents also agreed that Proven DSR should only be able to access one-year agreements, to be consistent with arrangements for existing generating CMUs.

Those opposed felt DSR was unsuited to multi-year agreements, particularly 15-year agreements, as it could not guarantee its availability that far in the future. A few respondents thought DSR should not be allowed to access multi-year agreements at all because it has a higher risk of non-delivery compared to generation. One respondent suggested DSR should be divided into ‘behind-the-meter-generation DSR’ and ‘turn-down DSR’, and that only behind-the-meter-generation DSR should be able to access agreements up to 15-years, whereas turn-down DSR should only be able to access agreements up to 3 years.

A.2.1.1.2 Impact of allowing DSR to access multi-year agreements

The large majority of respondents thought there would be limited or no interest from DSR operators in the multi-year agreements, as DSR providers would struggle to reach the required capital expenditure (‘CAPEX’) thresholds. A number of respondents noted that the only form of DSR that might be able to reach the CAPEX thresholds is behind-the-meter-generation, such

[9] For example: the exit bid submitted, the amount of unproven DSR capacity entered into the auction and the bidding strategy during the auction.

as battery storage. Therefore, some thought that the proposals may incentivise this form of DSR over others. Several respondents highlighted the need to monitor the impacts of the changes carefully to ensure that no unintended consequences arise.

A number of respondents expressed views on the CAPEX thresholds and their impact on DSR interest in multi-year agreements. Some thought the CAPEX thresholds should be kept under review and that the Government should consider lower thresholds for DSR, as this would increase participation. A few respondents felt that, due to the nature of DSR as a low CAPEX technology, determining access to multi-year agreements on the basis of CAPEX thresholds was unsuitable for DSR, and that there would be greater interest in multi-year agreements amongst DSR providers if access was based on criteria other than CAPEX. These respondents thought the Government should consider the positive impacts of allowing DSR to access multi-year agreements on market liquidity and the business cases of flexibility providers of allowing access to multi-year agreements. Other respondents thought that it was important that DSR be subject to the same CAPEX thresholds as Prospective Generation, to maintain technology neutrality.

Views on the impact that access to multi-year agreements would have on DSR bidding behaviour were mixed. A few respondents thought that DSR seeking multi-year agreements ('Multi-year DSR') would require higher clearing prices to come forward than DSR seeking one-year agreements ('One-year DSR'), due to the higher Credit Cover requirements. Others thought Multi-year DSR would be able to bid lower than One-year DSR as the administrative burden of prequalifying for the capacity auctions every year would be reduced.

A.2.1.1.3 The definition of CAPEX for DSR

A small majority of respondents favoured the Government's proposal to amend the definition of CAPEX to refer to Plant, Property and Equipment (as defined in International Accounting Standard 16 (IAS16)) which has the *primary purpose of delivering capacity.* However, a number of respondents opposed the change as they thought the existing definition was sufficient and that Independent Technical Experts (ITEs) would be able to account for any misapplications. Some were concerned that ITEs would have to learn how to apply the new definition and this would create inefficiencies and confusion. There were also concerns that the change could inadvertently reduce the scope of the definition of CAPEX for Prospective Generating CMUs, particularly with regard to pre-development and site preparation costs. Further clarity on the definition change was requested by a number of respondents, to ensure that non-DSR CMUs will not be affected by the change. One respondent requested clarification on whether the definition change would apply retrospectively to CMUs that already have an agreement.

A few respondents that the proposed definition would favour behind-the-meter-generation DSR relative to turn-down DSR. One respondent highlighted the importance of thorough checks by ITEs, as allowing DSR providers to include communications, metering and control equipment in their CAPEX could create opportunities for gaming given these costs are set by aggregators.

A.2.1.1.4 The application of the CAPEX thresholds for DSR

A majority of respondents favoured the proposed application of the CAPEX thresholds for DSR at CMU level rather than component level. Those opposed felt that all components in a DSR CMU should be required to exceed the threshold to ensure a level playing field with generation. A few respondents noted that applying the threshold at component level would be complex and create a barrier to entry for smaller providers.

A majority of respondents agreed that the CAPEX associated with individual DSR components should be reported to provide evidence for the application of thresholds at CMU level. Those that disagreed felt this went against the principle that DSR should be considered as the sum of its parts rather than as individual components. One respondent noted it should be possible to copy across costs for multiple similar components.

A.2.1.1.5 The 77-month cut-off date and Total Project Spend

A majority of respondents supported the proposed application of a 77-month cut-off date for DSR, in order to align with New Build generation, and agreed that the risk of potential gaming through component reallocation was covered through the proposed changes to the evidence of Total Project Spend milestone for DSR. However, a number of respondents noted that the 77-month cut-off date was defined for specific circumstances when the CM was first introduced (to avoid a hiatus in investment) which no longer apply to any CMUs and so should be revised. Several respondents suggested the cut-off date for all CMUs should be amended and tied to the date of the auction results day, in line with existing arrangements for Refurbishing CMUs. Two respondents felt that, whilst the rationale for 77 months no longer applied, the cut-off date was working fine for all CMUs and it was reasonable to allow the inclusion of some predevelopment costs.

Views were mixed on whether DSR components which had previously been entered into the CM should be able qualify as part of a DSR CMU with a multi-year agreement. Some respondents thought this should not be allowed, as it is not permitted for Prospective Generating CMUs. Others felt that it should be allowed as DSR is different to generation in that the equipment generally existed before the CM bid and component reallocation during the Delivery Year is permitted.

One respondent asked for clarification on whether a Multi-year DSR CMU that has failed to meet the CAPEX threshold at the Evidence of Total Project Spend milestone and is subsequently reduced to a one-year agreement can subsequently enter the CMU for a multi-year agreement.

A.2.1.2 Government response

A.2.1.2.1 Allowing DSR to access multi-year agreements

In line with the commitment recorded in the Commission's Decision,[10] the Government intends to allow Unproven DSR to access the same multi-year agreements as currently available to Prospective Generating CMUs (up to 3 years and up to 15 years), subject to meeting the relevant CAPEX thresholds. Whilst we accept that the majority of DSR projects may not incur high CAPEX, the participation of DSR in the CM auctions is increasing and it cannot be excluded that, in the future, some DSR providers may incur CAPEX at levels corresponding to the thresholds. Therefore, to ensure that, in the future, DSR capacity meeting these thresholds will not be prevented from accessing multi-year agreements, we are committed to allowing eligible DSR to access multi-year agreement lengths.

To enact this, will amend the definitions of 15 and 3 year minimum £/kW threshold in Regulation 11(3) and the definitions of Maximum Obligation Period, Qualifying £/kW Capital

[10] https://ec.europa.eu/commission/presscorner/detail/en/ip_19_6152

Expenditure, Total Project Spend and Capital Expenditure in Rule 1.2, to include Unproven DSR CMUs.

We intend to mitigate the risk of non-delivery and/or DSR providers speculatively bidding for multi-year agreements by increasing Credit Cover requirements and requiring additional information at Prequalification for Multi-year DSR. See Section A.2.2 below. As for the suggestion to split DSR into behind-the-meter-generation DSR and turn-down DSR, we feel this would be overly restrictive and prevent DSR providers from using a combination of both types of components in their portfolios.

A.2.1.2.2 Government assessment of impacts of allowing DSR to access multi-year agreements

See Annex 2.1.1.

A.2.1.2.3 The definition of CAPEX for DSR

In line with the majority view of respondents, the Government intends to proceed with amending the definition of CAPEX in Rule 1.2 for all CMUs to refer to IAS16 only for Plant, Property and Equipment which has the *primary purpose of delivering capacity.* This will ensure that DSR CMUs are not able to include inappropriate CAPEX in their Total Project Spend; for example, the CAPEX of air conditioning or freezer units which are turned down by DSR operators in order to deliver capacity. We are enacting the change for all CMUs to ensure consistency and technology neutrality. This change will apply to agreements awarded in future auctions only and will not apply to existing agreements.

We note the concerns that this may inadvertently reduce the scope of the definition of CAPEX for non-DSR CMUs. This is not our intention. We intend that non-DSR CMUs should be able to continue including the same costs in their Total Project Spend as they did under the previous definition. We also note the concerns around creating confusion amongst Capacity Providers and ITEs. To mitigate this, we will produce a guidance document to provide clarification on how the new definition should be applied. The Delivery Body will host this guidance on their website and share it with Capacity Providers during Prequalification.

The CAPEX values reported by DSR providers in relation to their components will be checked at the Evidence of Total Project Spend milestone by an ITE, in the same manner as is currently done for Prospective Generating CMUs (see Section A.2.3). This should reduce the risk of inaccurate figures being reported by the operator.

A.2.1.2.4 The application of the CAPEX thresholds for DSR

In line with the majority view of respondents, the Government intends to proceed with the proposal to apply the CAPEX thresholds for DSR at CMU level rather than component level. This will maintain consistency with requirements in place for Prospective Generating CMUs and better align with the principle that DSR should be treated as the sum of its parts rather than as individual components. We will enact this through an amendment to the definition of Qualifying £/kW Capital Expenditure in Rule 1.2.

We also intend to introduce a requirement that CAPEX should be separated into components for DSR when reporting an estimate of the Total Project Spend at Prequalification (see Section A.2.2) and the confirmed value of Total Project Spend at the Evidence of Total Project Spend milestone (see Section A.2.3). Whilst we recognise that this is not required for Prospective Generating CMUs, due to the nature of DSR (which can contain multiple components spread

A.2.2 Prequalification, Credit Cover and the Extended Years Criteria

Consultation question 3:

Do the proposed additional checks at Prequalification provide sufficient certainty that the CAPEX thresholds will be met by Unproven DSR? If not, what additional requirements should be applied at Prequalification?

Consultation question 4:

Is the proposed increase in Credit Cover for Unproven DSR bidding for a multi-year agreement suitable for ensuring that these CMUs will be committed to delivering their capacity, and will it prevent Unproven DSR from speculatively bidding for multi-year agreements?

Is there a need to consider, in addition to increased Credit Cover for Unproven DSR bidding for a multi-year agreement, draw down of Credit Cover for Unproven DSR that has its agreement length reduced?

Consultation question 5:

Should the Extended Years Criteria be applied to DSR? If so, how could it be applied to turn-down DSR?

Consultation question 6:

Are the proposed arrangements for a partial release of Credit Cover suitable for incentivising Unproven DSR with a multi-year agreement to make early progress towards delivery? Is there anything we could change to improve the incentive? Do you agree that Unproven DSR with multi-year agreements should not have to provide progress reports, as is required of generation?

A.2.2.1 Summary of responses

23, 23, 23 and 18 respondents provided responses to Questions 3, 4, 5 and 6 respectively.

A.2.2.1.1 Prequalification

A majority of respondents thought the proposed additional checks at Prequalification for Multi-year DSR were suitable and agreed with the principle that the checks should be aligned as far as possible with those already in place for Prospective Generating CMUs.

Those that disagreed felt the additional checks did not go far enough and that Multi-year DSR (particularly behind-the-meter-generation) should be subject to exactly the same requirements as Prospective Generating CMUs. One respondent thought it was unreasonable to ask DSR providers to declare at Prequalification whether or not their Unproven DSR CMU was expected to contain a storage component as this would not be known at that point in time.

A.2.2.1.2 Credit Cover

A large majority of respondents agreed with the proposed increase in Credit Cover for Multi-year DSR. They highlighted the need to discourage speculative bidding for multi-year agreements and ensure alignment with New Build CMUs. Those that disagreed felt the existing level of Credit Cover for DSR (£5,000/MW) was sufficient. One respondent thought the requirement for £10,000/MW Credit Cover should be extended to One-year DSR.

Views were mixed on whether the risk of speculative bidding could be further reduced through a draw-down of Credit Cover for those Multi-year DSR CMUs that have their agreement length reduced for a failure to meet the relevant CAPEX threshold. Some felt this would not be consistent with New Build CMUs and that the increased Credit Cover already provided a sufficient disincentive. One respondent argued that a draw-down in Credit Cover would be excessive as the reduction of agreement length to one-year does not create security of supply risks given the Government's ability to secure replacement capacity in future auctions. Others thought it should be considered.

A.2.2.1.3 DSR partial Credit Cover release

There was general agreement that the proposal to allow a partial release of Credit Cover for Multi-year DSR in return for demonstrable component recruitment progress was suitable and would incentivise early progress on delivery.

Those that disagreed suggested any arrangements should more closely align with the Financial Commitment Milestones (FCM) for Prospective Generating CMUs, for example by making the DSR partial Credit Cover release milestone mandatory and increasing Credit Cover to £15,000/MW if it is not met in time. Several respondents felt that, rather than having a single point of Credit Cover release, Credit Cover should be released incrementally as components are recruited and that this should apply to all DSR CMUs, not just Multi-year DSR. A few respondents raised concerns about the ability of ITEs to verify progress. One respondent noted that the costs of an ITE are fixed and therefore might be disproportionately burdensome for smaller CMUs. Another respondent thought the proposed requirement for a declaration that components would not be moved out of the CMU after the partial Credit Cover release was too restrictive and would limit the number of operators making use of the partial Credit Cover release.

A majority of respondents agreed it was not necessary for Multi-year DSR to provide progress reports every six months. One respondent noted this could be very complex and costly for DSR CMUs with a large number of components, each owned by different customers. However, a few respondents felt progress reports should be required for DSR, to align with requirements for Prospective Generating CMUs.

A.2.2.1.4 The Extended Years Criteria

Views were mixed about whether an equivalent to the Extended Years Criteria should be applied to Multi-year DSR. There was a general agreement that the application of the Extended Years Criteria in its current form to DSR, in particular turn down DSR, is challenging. A slight majority felt that it should be applied to ensure consistency with Prospective Generating CMUs. A few provided suggestions for how this could work.

- A declaration from DSR providers stating that the equipment (whether turn down or behind-the-meter-generation) is new and will be in place and maintained for the duration of the agreement.

- For turn-down DSR, the criteria could be applied to the underlying process that is being turned down, to ensure that the equipment is new and being maintained regularly.
- Individual sub-metering of DSR components could be carried out, to ensure DSR equipment performance can be distinguished from changes in site demand.
- There could be a distinction made between behind-the-meter DSR and turn-down DSR. The criteria could then be applied only to behind-the-meter DSR.

Those that felt the Extended Years Criteria should not be applied to Multi-year DSR noted that, for turn down DSR in particular, the capacity provided relates to the site's demand rather than equipment quality. Therefore, the importance of the DSR equipment being new and maintained was less relevant than for generation. Several respondents questioned how the Extended Years Criteria would interact with component reallocation. They also noted that satisfactory performance requirements in the Rules already provided a strong incentive to maintain capacity over the duration of the agreement, with component reallocation and secondary trading providing a mechanism to deal with any missing capacity. One respondent questioned whether the Extended Years Criteria was necessary for any CMUs.

A.2.2.2 Government response

A.2.2.2.1 Prequalification

We intend to implement the proposed additional Prequalification checks for all Multi-year DSR CMUs, in line with the majority view of respondents. This includes confirmation of the Maximum Obligation Period of the CMU, an estimate of Total Project Spend (broken down into components), an expanded Business Plan and a declaration on whether the CMU contains or is expected to contain a storage component. An additional declaration that was not mentioned in the original proposal will also be required: that the Applicant acknowledges that any Capital Expenditure incurred in respect of a DSR CMU Component which was used to obtain a multi-year agreement in another CMU, will not form part of the Total Project Spend of their CMU. This is to mitigate any risk of gaming through component reallocation (see Section A.2.5).

As explained in the consultation, we have endeavoured as far as possible to align the Prequalification requirements for Multi-year DSR with Prospective Generating CMUs. However, there are some circumstances in which it is necessary to make different provision, due to the nature of the two types of capacity and how they acquire their capacity (construction vs. component recruitment). For example, it is not appropriate to require Multi-year DSR to provide planning consents. The proposed additional checks strike the correct balance between mitigating speculative bidding and avoiding constraining the inherently uncertain nature of Unproven DSR at Prequalification.

We recognise that the declaration on whether any of the components of the CMU comprises, or is expected to comprise, a storage component (as defined as a storage facility in the Regulations) will require a Prequalification applicant in relation to a Multi-Year Unproven DSR CMU to take a view on the likely make-up of the CMU earlier than is typical for Unproven DSR. However, this is unavoidable as Multi-year DSR that contains storage will be de-rated differently to Multi-year DSR that is not declared as containing storage (see Section A.2.4). It is essential that the De-rating Factor, and bidding capacity, of the DSR CMU, is correctly identified at Prequalification.

To implement this proposal, where a Prequalification applicant in relation to a Multi-Year Unproven DSR CMU submits a declaration as part of Prequalification which confirms that the

CMU comprises, or is expected to comprise, a storage component, then the application will need to specify the appropriate storage duration class to be applied to the CMU. If a CMU is subsequently determined to comprise a storage component which was not declared at pre-qualification, then the CMU will be terminated under Rule 6.10.1(o). Ofgem can take further action based on this termination event if they suspect fraud.

In the Rules, the additional requirements for Multi-year DSR will be listed in the information to be included in the DSR business plan (Rule 3.10.1).

In response to stakeholder concerns around the potential to game the Total Project Spend milestone through component reallocation (see Section A.2.5), an additional declaration will be needed from Multi-year DSR CMUs at Prequalification. This declaration will require the Applicant to confirm that if the CMU contains or goes on to contain component(s) that has already been in another CMU with a multi-year agreement at the time of the Evidence of Total Project Spend milestone for that CMU, then the CAPEX of those component(s) will be listed as £0/kW in the ITE certificate provided at the Evidence of Total Project Spend milestone. A note should be included in the certificate that explains that the component was previously in a Multi-year DSR CMU, and there has not been included in the calculation of Total Project Spend. If the Delivery Body finds that the CAPEX of such a component has not been listed as £0/kW in the ITE certificate, then the CMU will be terminated under Rule 6.10.1(o).

Multi-year CMUs are currently allowed to submit a Duration Bid Amendment (Rule 5.6.4) in the capacity auction. This reduces the length of the agreement they are bidding for to one-year. We have considered whether such a provision is needed for DSR. Currently, as Unproven DSR CMUs are treated as ‘empty vessels’ at the time of Prequalification, DSR providers have the flexibility that the Duration Bid Amendment is designed to offer. Moreover, the Duration Bid Amendment would be administratively complex to facilitate for Multi-year DSR, as there are differing processes for One-year DSR compared to multi-year (e.g. Credit Cover and the partial Credit Cover release). It would be especially complex to facilitate for Multi-year DSR that contains a storage component, as One-year DSR that contains a storage component will have a different derating factor to Multi-year DSR that contains a storage component (see Section A.2.4) and therefore a different capacity obligation. We also note that no respondents to the consultation identified the Duration Bid Amendment as important for DSR. On this basis, we have decided it is not necessary or practicable to implement the Duration Bid Amendment for Multi-year DSR. For the same reason, Multi-year DSR will not be able to declare an agreement length of one-year when they select the agreement length that they will be bidding for 10 to 15 working days ahead of the auction (Rule 5.5.14).

A.2.2.2.2 Credit Cover

In line with the majority view of respondents, the Government intends to amend Regulation 59(2) to increase the Credit Cover requirement for Multi-year DSR to £10,000/MW. This will help discourage speculative bidding for the multi-year agreements and ensure alignment with Prospective Generating CMUs. The Credit Cover requirement for One-year DSR will remain at £5,000/MW.

We will not implement the suggestion made by some stakeholders for a draw-down of Credit Cover in instances where Multi-year DSR has its agreement length reduced as it has not reached the relevant CAPEX threshold. The increase in Credit Cover and additional deliverables required at Prequalification should be sufficient to mitigate the risk of speculative bidding.

A.2.2.2.3 DSR Partial Credit Cover Release

In order to more closely align the length of time for which Credit Cover must be maintained for Multi-year DSR with New Build CMUs, and to create an incentive for Multi-year DSR to make early progress in recruiting components in exchange for a reduction in Credit Cover, the Government intends to create an optional interim Credit Cover release milestone for Multi-year DSR which will be termed in the Regulations and Rules as the "DSR Partial Credit Cover Release". This will allow £5,000/MW of Credit Cover to be released if a prequalified applicant or CMU has demonstrated 50% progress towards the recruitment of capacity for their CMU. Like the Financial Commitment Milestone (FCM), the release can be met before the date on which Credit Cover must be posted (which is before the capacity auction), meaning a Multi-year DSR CMU may only ever need to post £5,000/MW Credit Cover. This change is in line with the majority view of respondents to the consultation.

A new rule will be inserted into the Rules (Rule 6.7B) which details the release, including the deliverables that must be submitted to the Delivery Body. This will include an updated version of the recruitment strategy contained in the Business Plan submitted at Prequalification (only the section on the recruitment strategy will need to be updated, not the declarations etc.) to demonstrate how the recruitment strategy has progressed. A declaration will also be required confirming that at least 50% of the CMU's capacity has been recruited and that this capacity will not be moved out of the CMU until the Notifying DSR Components milestone is complete (8.3.3A). And finally, an ITE certificate will need to be provided, verifying that the information submitted to meet the requirements of DSR Partial Credit Cover Release is accurate. Changes are also intended to be made to Regulation 59 (requirement to provide applicant Credit Cover) to require the amount of Credit Cover to be reduced where the requirements for DSR Partial Credit Cover Release are met.

We recognise that some respondents believe that arrangements for Multi-year DSR should more closely mirror the FCM for Prospective Generating CMUs. However, as for the requirements surrounding Prequalification, there are certain areas, including this one, in which we consider it is necessary to treat DSR differently due to the differing nature of the technologies. An FCM milestone would significantly restrict DSR recruitment, which can happen any time between the auction and the Delivery Year. The proposed change strikes the right balance between allowing flexibility in recruitment whilst rewarding early delivery for Multi-year DSR.

We recognise the concerns about the disproportionate cost of engaging ITEs for small operators. However, it is essential that there is independent verification before Credit Cover is released. Therefore, we will be maintaining the ITE requirement as part of the Partial Credit Cover Release for Multi-year DSR. This is consistent with requirements for Prospective Generating CMUs at the FCM. We will also be maintaining the requirement for components to be fixed between the Partial Credit Cover Release and the DSR Test, to avoid opportunities for DSR providers to use the same component/s to achieve the Partial Credit Cover Release for multiple CMUs.

We do not intend to require Multi-year DSR to provide progress reports every six months, in line with the majority view of respondents. Whilst this is not consistent with the requirements for Prospective Generating CMUs, regular progress reports do not necessarily provide useful insight into delivery progress for DSR as component recruitment is not a linear process and can take place close to the start of the Delivery Year.

A.2.2.2.4 The Extended Years Criteria

We do not intend to apply the Extended Years Criteria to Multi-year DSR. Whilst this is not consistent with the majority view of respondents, we note that the majority did agree that it would be problematic to apply this requirement to DSR, especially turn down DSR. We have considered the recommendations made by respondents on how the criteria could be applied to DSR. Whilst the criteria may be more suitable for behind-the-meter generation than turn-down DSR, a single DSR CMU can contain both types of components and we do not wish to constrain DSR by separating it into turn-down and behind-the-meter-generation, therefore we have not taken this option forward. As the capacity that can be delivered by a turn-down DSR site is more closely linked to the demand of the site than the age or maintenance of the equipment, we also do not think it would be appropriate to apply the Extended Years Criteria to the control equipment used to turn down demand, or to the underlying equipment that is creating the demand. We are satisfied that current arrangements for DSR, including SPDs, secondary trading and component reallocation, can mitigate the risk of non-delivery over the course of a 15-year agreement.

A.2.3 The Long-stop Date, Evidence of Total Project Spend and the Minimum Completion Requirement

Consultation question 7:

Is the proposed application of the Long-stop Date to Unproven DSR CMUs with a multi-year agreement suitable? Are there any risks or unintended consequences that we should be aware of?

Consultation question 8:

Is the proposed application of the Evidence of Total Project Spend milestone to Unproven DSR CMUs with multi-year agreements suitable, in particular the requirement to componentise costs?

Are there any risks or unintended consequences due to the Evidence of Total Project Spend occurring after the start of the Delivery Year and DSR CMUs being able to reallocate components?

Consultation question 9:

Do you agree that Unproven DSR with multi-year agreements should not be able to increase their capacity obligation after the DSR Test, or be subject to a Minimum Completion Requirement? Please provide reasons. Are there any unintended consequences that may arise from this proposal?

A.2.3.1 Summary of responses

20, 19 and 16 respondents provided responses to Questions 7, 8 and 9 respectively.

A.2.3.1.1 The Long-stop Date

A large majority of respondents directly supported the proposal to grant Multi-year DSR a 12-month extension to their milestones, to achieve consistency with the Long-stop Date for New Build Generating CMUs. One respondent was concerned about what happens if one delayed component prevents the whole DSR CMU from meeting a deadline and suggested that there could be an initial DSR Test carried out without the missing component.

A.2.3.1.2 The Evidence of Total Project Spend

A majority of respondents agreed with the proposed application of the Evidence of Total Project Spend milestone to Multi-year DSR, including the componentisation of CAPEX. As for Question 8, those that disagreed with the componentisation of CAPEX did so because they thought it went against the principle of treating DSR as the sum of its parts rather than individual components, and that it was inconsistent with arrangements for Prospective Generating CMUs.

Several respondents highlighted the need for robust monitoring to ensure component reallocation is not used to game the Evidence of Total Project Spend milestone by using one high capex component to attain a multi-year agreement in relation to more than one DSR CMU. One respondent suggested that there should be an explicit question when a component is registered with the Delivery Body to identify whether the component had previously been in a Multi-year DSR CMU. Another respondent thought that equipment serial numbers would need to be collected to identify DSR components as metering information was not sufficient.

Several respondents argued that Multi-year DSR should not be allowed to reallocate components between the DSR Test and the Evidence of Total Project Spend milestone to avoid opportunities for gaming.

A few respondents raised concerns about the ability of ITEs to verify progress. One respondent noted that the costs of an ITE are fixed and therefore might be disproportionately burdensome for smaller DSR CMUs.

Two respondents thought that any Multi-year DSR CMU which has its agreement length reduced to one-year at the Evidence of Total Project Spend milestone, as a result of failing to meet the CAPEX thresholds, should be subject to a termination fee and/or draw down of Credit Cover.

A.2.3.1.3 Increases in Capacity Obligation and the Minimum Completion Requirement

A majority of respondents agreed that it was not necessary to allow Multi-year DSR to increase their capacity obligation after the DSR Test. One respondent noted an operational concern that the DSR Test is time consuming, so is impractical to repeat. Those who disagreed felt that arrangements should be aligned with those already in place for Prospective Generating CMUs. One respondent thought that no CMUs should be able to increase their capacity obligation after either the SCM or the DSR Test.

Views were mixed on whether the Minimum Completion Requirement (MCR) should be applied to Multi-year DSR. A small majority felt it was not necessary, as DSR only has to demonstrate greater than 2MW capacity in the DSR Test in order to avoid termination (this will be reduced to 1MW once the Minimum Capacity Threshold is reduced – see Section A.3). Those who disagreed thought that arrangements should be aligned with those in place for Prospective

Generating CMUs, to preserve technology neutrality. One respondent thought that Termination Events and Termination Fees should be aligned between Prospective Generating CMUs and Multi-year DSR.

A.2.3.2 Government response

A.2.3.2.1 The Long-stop Date

In line with the majority view of respondents, the Government will implement a 12-month extension to the deadlines for the DSR Test, Notifying DSR Components, Metering Assessment and Metering Test for Multi-year DSR. This will mirror the effect of the Long-stop Date for New Build generating CMUs. These extensions will be added to the declarations in Rule 3.10.2. They have also been noted in the relevant section of the Rules covering the (Joint) DSR Test (Rules 13.2 and 13.2B), the Metering Assessment and the Metering Test (Rules 8.3.3 and 13.3.2A).

Credit Cover will need to be maintained as appropriate until the DSR Test is complete. Credit Cover will continue to be released or drawn down in the same manner, depending on the amount of proven capacity at the DSR Test. If the DSR Test is not completed by one-month before the start of the second Delivery Year, then the CMU will be terminated. Termination arrangements, including fees, for Multi-year DSR will remain the same as for Unproven DSR with one-year agreements.

If these extensions are utilised, Capacity Payments will not be made to the Multi-year DSR CMU until the DSR Test, Metering Assessment and Metering Test (if needed) are complete. A new rule will be added which details the requirements that must be met for a Multi-year DSR CMU's Capacity Agreement to take effect (Rule 6.7A).

In relation to the concerns about single components holding up the DSR Test, we do not intend to pursue the suggestion to allow an initial DSR Test to be carried out without the missing component. We note that the DSR Test can be passed and the agreement become active with less than the capacity obligation, provided the total capacity of the CMU is greater than the Minimum Capacity Threshold. If components are late then this option can be taken to avoid termination.

The deadline for the Evidence of Total Project Spend milestone will be the same for Multi-year DSR as for Prospective Generating CMUs (i.e. up to 3 months after the start of the first Delivery Year, or on the date that the agreement takes effect if the extensions are used). The deadline for Notifying DSR Components (8.3.3A) does not need to be updated, as it is tied to the deadlines of the Metering Assessment and DSR Test.

A.2.3.2.2 The Evidence of Total Project Spend

In line with the views of respondents, the Government will implement the Evidence of Total Project Spend for DSR in the same way as the milestone currently applies to Prospective Generating CMUs, with the exception that Multi-year DSR will also be required to break the Total Project Spend into components. This will include the requirement for an ITE certificate. These will be implemented through changes to Rule 8.3.6.

Whilst we recognise that the componentisation of costs is not required for Prospective Generating CMUs, and agree generally with the principle that DSR CMUs should be treated as the sum of its parts, greater transparency on CAPEX is essential for enabling the ITE to

A.2.4 Storage and DSR

Consultation question 10:

Will the proposed amendment suitably clarify our policy intent and address the issue of stand-alone storage units being entered into the CM as DSR CMUs?

Consultation question 11:

Are there any unintended consequences that may arise as a result of applying storage De-rating Factors and requiring extended performance testing for DSR CMUs with multi-year agreements that contains behind-the-meter storage components? Is our proposal to check whether these CMUs contain a storage component through a declaration at Prequalification suitable?

A.2.4.1 Summary of responses

24 and 21 responses were received for Questions 10 and 11 respectively.

A.2.4.1.1 Stand-alone storage units entering the Capacity Market as DSR

Question 10 sought views on the proposed amendment to the description of DSR in CM legislation. The proposal is to clarify that, for DSR, the baseline of imported electricity below which metered volumes are reduced cannot be primarily composed of electricity used to charge a storage unit. The purpose of the proposal is to make it clear that stand-alone storage units should not be entered into the CM as DSR.

The majority of respondents were supportive of the proposed amendment and felt it suitably clarified the policy intent.

One respondent raised objections to the proposal on grounds that stand-alone batteries can deliver contributions to security of supply that are similar to DSR, provided they are combined with another technology.

Another respondent felt the proposals were suitable but didn't go far enough, and that a declaration should be required from DSR CMUs stating that they do not contain any generating units which contain stand-alone storage (i.e. do not meet the definition of a permitted on-site generating unit). This should then be checked by the Delivery Body at the Metering Test. Similarly, another respondent felt there should be a robust and evidence-based test to ensure storage units are not creating a false demand baseline, so as to appear as a DSR CMU.

Several respondents queried what would happen to those CMUs that may already have won agreements in previous auctions as DSR and contain stand-alone storage components. They felt that the changes should apply retrospectively, and that the Delivery Body should be taking action to terminate those CMUs. A number of respondents noted that the Government and the Delivery Body had previously communicated their position on the issue, including in the 2019 CM launch event documentation. One respondent also noted their belief that the policy intent had already been sufficiently clear in the Regulations.

Several respondents noted the importance of ensuring that the phrasing of the amended definition of DSR is comprehensive and clear to prevent further gaming. Several respondents

highlighted that care should be taken to define the term ‘primarily’ so CM participants would be sure if their component met the criteria. A similar point was raised by another respondent, stressing the term should not inadvertently prevent certain legitimate forms of DSR in the future e.g. electric vehicle modulation. A further respondent stated the term ‘primarily’ may not be robust enough, noting a site with a nominal load could be paired to large stand-alone storage units. The respondent suggested imposing a 50% threshold for the proportion of a DSR customer’s demand that can be comprised of charging storage.

Several respondents questioned how the revised policy intent would be monitored and enforced and what steps the Delivery Body would take to ensure compliance. Similarly, a few respondents questioned what steps would be taken if a DSR CMU was found to contain one or more stand-alone storage components. Three respondents felt that strong penalties, including termination fees, repayment of any CM revenues and a ban from entering future CM auctions, should apply to any DSR CMUs found to contain a stand-alone storage unit.

A.2.4.1.2 Behind-the-meter storage units in Multi-year DSR CMUs

Question 11 sought views on applying storage De-rating Factors and Extended Performance Testing for Multi-year DSR CMUs.

There were mixed responses to this question. A number of respondents were in favour of the proposal and thought they were proportionate, given the risk of gaming. However, a number of respondents felt the proposals were disproportionately restrictive and that Unproven DSR applicants would not know for certain whether their CMU would contain a storage component at Prequalification. Those opposed instead favoured the inclusion of a threshold level (e.g. 50%) of storage within a Multi-year DSR CMU before a storage de-rating is applied and/or De-rating Factors set in proportion to the amount of storage in the CMU. They thought this approach would enable greater flexibility in a DSR CMU’s configuration. One respondent recommended excluding CAPEX associated with storage components from the Total Project Spend of Multi-year DSR, as a way to ensure that Multi-year DSR does not include high proportions of storage, rather than the making changes to de-rating and requiring Extended Performance Testing. Another suggested that De-rating Factors for Multi-year DSR CMUs could be adjusted just before the Delivery Year, once they have confirmed whether they contain a storage component.

Some respondents expressed concern that the proposed changes to de-rating and the Extended Performance Test would be extended to include One-year DSR in the future. Conversely, some respondents felt the proposals should apply to both Multi-Year and One-year DSR. They argued that the more stringent rules for multi-year agreements would incentivise DSR CMUs to apply for one-year agreements where a more favourable De-rating Factor would be applied. They also noted that behind-the-meter storage is not necessarily the only form of duration-limited DSR.

A number of respondents raised questions about how the proposed requirements would be enforced and what mechanism would be in place to verify the declaration on whether a Multi-year DSR CMU contains a storage component. One respondent suggested that an ITE report should be required in addition to a declaration. Another respondent thought that Multi-year DSR CMUs should be closely monitored for storage components, with additional due diligence undertaken by the Delivery Body. They also questioned how component reallocation would work for Multi-year DSR that contains a storage component.

Two respondents were concerned that the proposals could accidently capture commonly used power configurations as storage e.g. uninterruptible power supplies or back-up batteries on a

A.2.5 Multi-year DSR component reallocation and secondary trading

Consultation question 12:

Is the proposal to restrict each DSR component to being used only once to meet Evidence of Total Project Spend requirements sufficient to prevent gaming through component reallocation?

Do we need consider preventing DSR with multi-year agreements from reallocating components until the cut-off date has passed?

Consultation question 13:

If we allow DSR with multi-year agreements to reallocate components, is the proposal for an annual repeat of the DSR Test for CMUs that have reallocated components (in line with current arrangements for DSR) suitable and are there any unintended consequences that may arise?

Consultation question 14:

Are there any unintended consequences which may arise from preventing Unproven DSR CMUs with a multi-year agreement from secondary trading until after completing the DSR Test?

A.2.5.1 Summary of responses

21, 19 and 18 respondents provided responses to Questions 12, 13 and 14 respectively.

A.2.5.1.1 Component reallocation

A majority of respondents agreed that it was important to manage the gaming risk created by component reallocation and supported the proposal to only allow the CAPEX of each DSR component to be used only once in relation to a Multi-year DSR CMU's Total Project Spend. Those that opposed the proposal thought that Multi-year DSR should not be allowed to reallocate components at all, as Prospective Generating CMUs are not able to do so. One respondent suggested that a director's declaration should be submitted that confirms that the DSR CMU's Total Project Spend does not include the CAPEX of any components previously used to obtain a multi-year agreement for another DSR CMU. Another respondent suggested that providers should be required to complete DSR Tests simultaneously for all their CMUs to help to prevent gaming through component reallocation.

Views were mixed on whether component reallocation should be prevented until the component would no longer be eligible for use in another Multi-year DSR CMU's Total Project Spend. Many thought this was not necessary, as the proposed restrictions on Total Project Spend sufficiently mitigated the risk of gaming. Other respondents felt that the cut-off date in the definition of Total Project Spend should be reduced from 77 months for Multi-year DSR to reduce the risk of gaming.

Views were mixed on how DSR components could be tracked. Whilst many recognised that metering information was not wholly sufficient for tracking individual components, a majority felt

that the collection of serial numbers would be very burdensome, particularly for small operators, and would be disproportionate to the risk. Two respondents suggested that, to reduce burdens, serial numbers should only be collected for components with a significant cost. One respondent highlighted that it would be very difficult to collect and audit serial numbers as there could be multiple serial numbers even for a single piece of equipment within a component. Another respondent thought that carrying out site visits would be more effective than collecting serial numbers.

A large majority of respondents supported proposals for a repeated DSR Test before the next Delivery Year if a CMU had engaged in component reallocation. One respondent noted that whilst annual testing made sense, testing after every reallocation should be avoided as it would be too burdensome. Another thought that the repeated test should only apply if reallocation has been used for a reason other than a failed component. One respondent was concerned that repeated testing could create a resourcing bottleneck for the Delivery Body if it were to happen at the same time for all Multi-year DSR CMUs.

A.2.5.1.2 Secondary trading

A majority of respondents agreed with the Government's proposal that Multi-year DSR should be prevented from secondary trading until after the DSR Test. One respondent thought that this restriction should also be extended to One-year DSR. Those that disagreed felt that it would prevent DSR operators from managing their risk profile by trading away capacity that they are unable fulfil by the DSR Test. Two respondents suggested that Multi-year DSR should be able to secondary trade only the first year of their agreement without completing the DSR Test, to allow additional time for delivery. One respondent thought that all CMUs should be allowed to secondary trade before the either the Substantial Completion Milestone (SCM) or DSR Test, as the risk of speculative bidding or gaming through secondary trading is limited.

A.2.5.2 Government response

A.2.5.2.1 Component reallocation

In line with the majority view of respondents, the Government will implement the proposal to only allow the CAPEX of a DSR component to contribute once to a Multi-year DSR CMU's Evidence of Total Project Spend. This should be sufficient to mitigate the potential for gaming, and therefore there is no need to consider further restrictions to component reallocation or the simultaneous testing of DSR CMUs. This will be implemented through additions to Rule 8.3.6. That said, we agree that it would be beneficial to require a director's declaration to the effect that the requirement will be followed. This will enable the Delivery Body to terminate any CMU which fails to comply with Rule 6.10.1(o). This declaration will be required for all Multi-year DSR CMUs at Prequalification and will be added to Rule 3.10.1 (see Section A.2.2). For Multi-year DSR, component reallocation will not be allowed until after both the DSR Test and the Evidence of Total Project Spend milestones are complete, to prevent potential gaming by bringing in different components for the two milestones.

We recognise the issues raised by respondents with tracking components using metering information and the importance of being able to uniquely identify DSR components in order to mitigate gaming. However, we also understand that the collection of serial numbers could be burdensome, particularly for small operators. In line with this, we intend to collect only one serial number for Multi-year DSR components at the Evidence of Total Project Spend milestone (in the ITE certificate) and the Notifying DSR Components milestone (submitted to the Delivery Body). This serial number should correspond to that assigned by the manufacturer to the piece of equipment within the component that makes up the highest share of CAPEX of

the component. This requirement strikes the right balance of ensuring that components can be uniquely identified, and risks of gaming are minimised, whilst minimising burdens on operators.

The serial number provided for each component within a Multi-year DSR CMU must be verified by the ITE and listed in the ITE certificate at the evidence of Total Project Spend milestone. We will enact this through changes to Rule 8.3.6. Multi-year DSR CMUs must also provide the serial number associated with each component in their CMU to the Delivery Body at the Notifying DSR Components milestone. This will ensure that the Delivery Body are able to maintain a database of component serial numbers against which they can cross reference the ITE certificates. We have enacted this through changes to Rule 8.3.3A. We will add a definition of a Manufacturer Serial Number to Rule 1.2, to ensure clarity. One-year DSR will not have to report serial numbers for their components.

If a component was previously used to obtain a multi-year agreement in another Multi-year DSR CMU, then the CAPEX of that component must be listed as £0/kW in the ITE certificate at the Evidence of Total Project Spend milestone and the reason for this noted in the certificate. The Delivery Body will cross check the serial numbers in the ITE certificate against the serial numbers provided by other Multi-year DSR CMUs at the Notifying DSR Components milestone. If they find that the CMU contains a component that was already used to obtain a multi-year agreement in another Multi-year DSR CMU and the CAPEX of this component is not listed as zero in the ITE certificate, the CMU will be terminated under Rule 6.10.1(o), as the declaration provided at Prequalification will have proven to be false.

Regarding suggested changes to the 77-month cut-off date, see our response in Section A.2.1.2.

Regarding calls amongst respondents for a repeat DSR Test at the end of each Delivery Year in which component reallocation has been carried out, the Government does not intend to introduce this requirement. Multi-year DSR CMUs have to complete SPDs on an annual basis, which provides sufficient assurance that these CMUs will maintain their capacity for the duration of the agreement. If Multi-year DSR CMUs are concerned about failing an SPD, then our preference is for them to utilise secondary trading. As for One-year DSR, Multi-year DSR CMUs that have engaged in component reallocation must repeat a DSR Test at least 1 month before the start of any subsequent capacity agreement. Rule 8.3.2A will be updated to enact this and Rule 8.3.4 will be amended.

In addition to component reallocation, there are two other situations in which a repeat DSR Test is currently required for DSR:

- If a metering change has been made to one or more components (which still requires a new DSR test). This must be completed by 6 weeks before the start of the next Delivery Year (Rules 13.2.12E and 13.2B.23); and
- Where the Settlement Body has identified a metering fault due to a change that has invalidated the Meter Test (Rules 13.2A or 13.2C apply).

For Multi-year DSR, we have amended the requirements in relation to the first situation above to be similar to component reallocation, i.e. a repeat DSR test is needed 6 weeks before the start of any subsequent agreement. We will implement this through changes to Rules 13.2.12, 13.2.12A, 13.2.12E (DSR Test) and 13.2B.18, 13.2B.18A and 13.2B.23 (Joint DSR Test). In relation to the second situation (metering faults) we will apply the current arrangements for DSR to Multi-year DSR, as this has additional ramifications including the pay back of CM revenues (see Rule 13A). We will, therefore, not make any changes to these Rules.

A.3 The Minimum Capacity Threshold

A.3.1 Summary of responses

Consultation question 16:

How much participation of CMUs sized 1-2MW do you expect there will be in future capacity auctions and what impact might this have on auction liquidity and price?

19 responses were received in relation to question 16.

A large majority of respondents thought that the reduction in the Minimum Capacity Threshold would have a limited impact on future capacity auctions. Several of these respondents noted that capacity units below the threshold can already enter the CM through aggregation and that aggregating into larger units can be more economic.

A few respondents felt the reduction of the Minimum Capacity Threshold could increase auction liquidity, resulting in a potential reduction in the clearing price. Respondents highlighted that the lower threshold could also enable smaller CHP or domestic units to be aggregated into a CMU and so now enter the CM. One respondent noted that with digitisation there was likely to be an increase in smaller, decentralised assets entering the CM. It was also noted that the lower threshold could enable smaller DSR components to participate in the auctions directly and so potentially submit lower exit bids, given they will no longer need to pay a percentage to aggregators.

A number of respondents touched on the administrative changes of the reduced threshold. One respondent noted that the reduction could reduce their administrative costs by allowing them to split aggregated components into separate CMUs, which can be consistently maintained over time rather than having to regularly reallocate components between CMUs. The respondent noted they own and maintain multiple, geographically dispersed smaller units and so do not benefit from the potential economies of scale from aggregating components, as noted by other respondents. Conversely, a couple of respondents noted that the administrative cost to the Delivery Body of facilitating the participation of a greater number of smaller units could outweigh the potential benefits.

Two respondents felt the reduction in the Minimum Capacity Threshold would benefit DSR providers and increase the volume of DSR able to access the market. The respondents noted smaller unit sizes are beneficial to DSR participation, and that smaller units have a reduced risk associated with the DSR Test, and SPDs in particular. Another respondent noted the change could improve the potential for secondary trading. Several respondents also suggested that smaller units operating independently i.e. without aggregation, would be more accountable for their own performance and not adversely affected by the performance of other components within an aggregated CMU which are not under their control.

One respondent welcomed the proposal to address the discrepancy between the Minimum Capacity Threshold and the threshold that applies to Secondary Trading. The respondent suggested there should be no Minimum Capacity Threshold applied for secondary trading, provided the whole Capacity Obligation of a CMU is traded.

Finally, one respondent questioned why the threshold had not been reduced to 0.5MW.

A.3.2 Government response

The Government welcomes the broad agreement from respondents that reducing the Minimum Capacity Threshold will not have adverse impacts on the CM auctions and could increase liquidity. The Government intends to amend Regulation 15(4)(a) to implement this reduction for entry to Prequalification.

We also intend to amend the Rules which refer to the value of the Minimum Capacity Threshold (currently 2MW), rather than referring to the defined term "Minimum Capacity Threshold": these appear in the context of setting the threshold to be met when completing the DSR Test (Rule 8.3.2) and where the DSR Test is required when addressing changes to metering (Rule 13A). These will be amended to refer to 1MW.

The Government does not believe it is necessary, at this stage, to further reduce the Minimum Capacity Threshold below 1MW, as participation at or near to the 1MW threshold is expected to be limited. As stated in the State aid Decision, we will reassess the threshold by October 2021 and consider the need for a further reduction.

For secondary trading, the minimum Capacity Obligation that can be traded is linked to the Minimum Capacity Threshold. However, for secondary trading, the threshold applies to the de-rated capacity of the CMU, whereas for prequalification it applies to the connection/DSR capacity. This means that some Capacity Providers are unable to take part in secondary trading.

In order to address this, the Government will amend Rule 9.2.4(a)(ii) so that secondary trading below the Minimum Capacity Threshold is permissible if the whole Capacity Obligation is being traded. Where the trade is for only part of a Capacity Obligation, the Minimum Capacity Threshold will still apply.

The reduction in the Minimum Capacity Threshold will mean some capacity units between 1MW and 2MW that were not previously eligible for the CM may become Mandatory CMUs.[12] Owners of Existing Interconnector CMUs or Existing Generating CMUs sized between 1MW and 2MW that meet the definition of a Mandatory CMU will be required to participate in the CM, unless they submit an opt-out notice to the Delivery Body.

See Annex 2.1.2 for an assessment of the impacts of reducing the Minimum Capacity Threshold.

[12] A Mandatory CMU is an existing interconnector or generating unit with capacity above, or equal to, the Minimum Capacity Threshold and which is required to participate in the CM, unless an opt-out notice is submitted (Rule 3.11).

A.4 The amount of T-1 set aside capacity

A.4.1 Summary of responses

Consultation question 17:

Are there any unintended consequences which may arise from formalising the 50% set-aside commitment and the 95% confidence interval methodology in legislation?

15 responses were received to question 17.

The majority of respondents supported providing a legislative underpinning to the 50% set-aside commitment and the 95% confidence interval methodology.

The commitment by Government to seek to procure at least 50% of the set-aside target capacity through the T-1 auctions was seen by some respondents as a key enabler for some technologies, which do not see the T-4 auction as a viable commercial proposition - such as DSR. There was support from some respondents for the Government to retain the maximum flexibility possible in setting the capacity targets for the CM auctions, stating that the T-1 set aside capacity should be able to respond to demand and the needs of the market. Others, however, highlighted that the T-1 set-aside needs to be bigger than is currently the case if it is to represent an attractive commercial opportunity for some technologies.

Amongst respondents opposed to this change, there was some recognition that the Government had committed to introduce this change as part of the Commission's Decision. However, they expressed concern that formalising the 50% set aside in legislation poses risks, most notably risking the over-procurement of capacity at T-1 auctions, increasing costs to consumers. Respondents cited the recent T-1 auction for the Delivery Year 2020/21 for which the demand curve adjustment report recommended a target capacity of 0MW, whereas over 1GW of capacity was procured in the auction.[13]

Given the small target capacity for the T-1 in 2020/21, and the risk of over-procurement from placing the 50% set-aside commitment in legislation, some respondents queried whether the split between the T-4 auction target capacity and the T-1 auction target capacity remains appropriate.

A.4.2 Government response

It remains the Government's intention to implement this commitment through a change in legislation, as set out in the consultation. We will amend Regulation 12 of the Regulations so that both the long-standing 50% set-aside commitment, and the methodology for determining the minimum amount of set-aside, as applied since 2016, are required to be applied as part of the auction parameter setting process for all future auctions. These amendments will also

[13] Report to Secretary of State - Adjustment to demand curve, T-1 auction 2020/21 Delivery Year

A.5 Incorporating new technologies into the Capacity Market

A.5.1 Summary of responses

Consultation question 18:

Are you aware of any new capacity types not currently participating in the CM which can effectively contribute to addressing the generation adequacy problem? If so, please provide details.

Consultation question 19:

Do you agree with the proposal to introduce a new duty on the Secretary of State to review annually whether there are any new capacity types, not currently participating in the CM, which can effectively contribute to addressing the generation adequacy problem? We would welcome your views on the scope and steps of the review itself.

A.5.1.1 New capacity technology types

15 responses were received in relation to question 18.

The majority of respondents stated they were unable to identify any new capacity technologies that are not currently eligible compete in the CM.

Three respondents did highlight capacity types they felt could potentially participate in the CM in future. One respondent highlighted hydro capacity (tidal, wave, and ocean current) as having potential to come forward in future. Another respondent requested a review of co-located assets as a new capacity type.

A.5.1.2 Annual review of new capacity types

18 responses were received in relation to question 19.

The majority of respondents supported the proposals to introduce an annual review to identify new capacity types not currently eligible to compete in the CM. Respondents felt the proposal was appropriate and would meet the desired outcome.

One respondent suggested the call for evidence should include guidance on the type of evidence that potential new capacity providers would need to submit in order to demonstrate they were able to make an effective contribution to security of supply. Another respondent felt the proposals would ensure potential new technologies were not missed, but that the Government and Delivery Body should already be considering new technologies as part of their ‘horizon scanning’ work. The respondent concluded that the proposed Call for Evidence should be ‘light touch’. Additionally, another supportive respondent felt potential providers should have the opportunity to propose new technologies outside of the Call for Evidence.

Three respondents opposed the proposals citing the additional administrative burden they would create. One of these respondents felt project developers can already apply to the Delivery Body for their new technology to be incorporated into the CM, without the need to create an additional burden on the Secretary of State to conduct an annual review. Another respondent advocated that project developers could indicate their interest within the annual Rules change process in order to examine the technology before a full review was conducted.

A.5.2 Government response

A.5.2.1 New capacity technology types

The Government recognises the very limited number of potential new technologies identified by respondents.

We note that 'hydro' generating units are already recognised as Generating Technology Class in the CM, although hydro generating units driven by tidal flows, waves, ocean currents or geothermal sources are currently excluded on the basis that project developers of these sub-categories have not come forward to express an interest for their inclusion in the CM. The proposed annual review process should enable their inclusion in future at the appropriate time.

Co-located assets, or Hybrid CMUs were raised in the Further Amendments to the CM Consultation in 2019.[17] The Government asked if the existing approach to enabling the participation of hybrid CMUs in the CM (including the approach to de-rating) was appropriate. All but one of the 26 responses felt the existing approach was appropriate. Our Five-year Review of the CM[18] also considered Hybrid CMUs and we agreed with the Further Amendments to the CM Consultation. Given the clear satisfaction with the current methodologies, we do not believe it is necessary to include hybrid CMUs as a new capacity type.

A.5.2.2 Annual review of new capacity types

The Government welcomes the broad support for the proposal. We will, therefore, move to implement the proposals outlined in the Future Improvements Consultation by inserting a new 'Rule 2.4 - Annual Review of Generating Technology Classes'.

The new provisions will require the Secretary of State, each calendar to year, to review whether any generating technology not currently competing in the CM should be eligible to compete in future auctions. The annual review process will commence with a Call for Evidence, published by 1 October, to consult interested parties on whether any generating technology not already identified as a Generating Technology Class has emerged which is capable of contributing to security of supply. By 1 December, the Secretary of State must publish the outcome of that Call for Evidence. If a new technology is identified, and evidence is provided that it could effectively contribute to security of supply, the Secretary of State must amend the Rules as soon as reasonably practicable to enable that technology to compete in future auctions. This could include directing the Delivery Body to develop and consult on an appropriate methodology for calculating De-rating Factor(s) for any new technologies.

[17] https://www.gov.uk/government/consultations/capacity-market-further-technical-amendments
[18] https://www.gov.uk/government/publications/capacity-market-5-year-review-2014-to-2019

A.6 Carbon emission limits reporting and verification mechanism

The Government first considered proposals for introducing the new carbon emission limits in the CM, as established in Article 22 of the Regulation (EU) 2019/943 of the European Parliament and of the Council of 5 June 2019 on the internal market for electricity (the "Electricity Regulation"), as part of the Summer 2019 Consultation. This sought views on: the date from which the emission limits should apply to existing capacity; whether constraints should be placed on the length of agreements awarded to Refurbishing CMUs participating in the auctions held in early 2020, and; the arrangements relating to the termination of Capacity Agreements and recovery of Capacity Payments. Section B outlines the Government Response to that consultation.

Subsequent to the Summer 2019 Consultation closing, an opinion containing a methodology for calculating the carbon emission limits was published by the Agency for the Cooperation of Energy Regulators (ACER) on 17 December 2019 (the "ACER opinion").[19] Building on the ACER opinion, the Government included in the Future Improvements Consultation further changes to the Rules to implement arrangements for reporting emissions and verifying the carbon emission limits. This section provides an overview of the responses received in relation to the proposals, as well as an explanation of the decisions taken by the Government in light of the responses.

A.6.1 Overall assessment of the mechanism

A.6.1.1 Summary of responses

Consultation question 20:

Do you agree with the proposed reporting and verification mechanism, outlined in this section? Please set out your reasons.

Consultation question 25:

Do you have any further comments or any suggestions on how the proposed emission limits reporting and verification mechanism could be improved?

24 respondents responded to Questions 20 and 25.

Overall, 13 respondents expressed an opinion on the reporting and verification mechanism proposed in the Future Improvements Consultation, which will include submission of an ex ante desk-based calculation of the carbon emissions of a generating unit with no ex post monitoring of real-world emissions. The responses received broadly agreed that the proposed mechanism is appropriate and fit for purpose, albeit there are aspects which could lead to

[19] Opinion No. 22/2019 https://www.acer.europa.eu/Official_documents/Acts_of_the_Agency/Opinions/Opinions/ACER%20Opinion%2022-2019%20on%20the%20calculation%20values%20of%20CO2%20emission%20limits.pdf

unintended consequences or warrant fine-tuning. A number of specific issues, concerns and alternative proposals were also flagged, which are described under the relevant subject area in sections A.6.2 to A.6.9 below.

A.6.1.2 Government response

The Government intends to implement the reporting and verification mechanism as described in the Future Improvements Consultation, with the refinements described in sections A.6.2 to A.6.9 below, by introducing a number of amendments to the Rules. In summary, the intended reporting and verification mechanism will operate as follows:

- **Existing Generating CMUs and Proven DSR CMUs:** During prequalification for auctions for the Delivery Year 2024/25 and beyond, an Existing Generating CMU or Proven DSR CMU which contains a Fossil Fuel Component[20] or a storage facility connected to a Fossil Fuel Component will be required to submit a Fossil Fuel Emissions Declaration to the Delivery Body. The Declaration must list all the Fossil Fuel Components in that CMU and specify the emissions of each component, together with supporting evidence, to demonstrate compliance with the Fossil Fuel Emissions Limit[21] or the Fossil Fuel Yearly Emissions Limit[22] (which was described in the Summer 2019 and Future Improvements Consultation as "the yearly limit").

  No declaration will be required at Prequalification from Existing or Proven DSR CMUs that do not contain a Fossil Fuel Component or a storage facility connected to a Fossil Fuel Component. However, if there is a material change to the CMU or a component comprised in that CMU subsequent to the award of the Capacity Agreement, such that the CMU will contain a Fossil Fuel Component or storage facility connected to a Fossil Fuel Component, a Fossil Fuel Emissions Declaration will be required as soon as reasonably practicable after the capacity provider becomes aware of the material change.

- **New Build CMUs, Refurbishing CMUs and Unproven DSR CMUs:** During Prequalification, applicants for New Build CMUs, Refurbishing CMUs and Unproven DSR CMUs will be required to submit a Fossil Fuel Emissions Commitment (which will be a new Exhibit in the Rules) undertaking that the relevant CMU will either not comprise of components (Fossil Fuel Component or a storage facility connected to a Fossil Fuel Component) which will not comply with the emission limits or if the CMU does contain a Fossil Fuel Component or storage facility connected to a Fossil Fuel Component, the relevant person will submit a Fossil Fuel Emissions Declaration at the milestone relevant to the CMU type (see Section A.6.2 below).

- **General requirements:** A CMU will not prequalify unless a Fossil Fuels Emissions Declaration or Fossil Fuel Emissions Commitment which meets the requirements in the Rules is provided where required and, in the case of a Fossil Fuels Emissions

[20] As will be defined in Rule 1.2.1.
[21] Will be defined in Rule 1.2.1 to align with Article 22(4) of the Regulation to mean "550g of carbon dioxide of Fossil Fuel origin per kWh of electricity generated".
[22] This will be defined in Rule 1.2.1 to mean "350 kg CO_2 of Fossil Fuel origin on average per year per installed kWe"

Declaration, demonstrates that no component does not comply with the Fossil Fuel Emissions Limit (or, if relevant, the Fossil Fuel Yearly Emissions Limit).

Fossil Fuel Emissions Declarations will need to be signed by two directors. The emissions of components specified in a Fossil Fuel Emissions Declaration with an "Installed Capacity"[23] above 1 MW[24] must be verified by an "Independent[25] Emissions Verifier". We are aware that there is a risk of there being limited availability of Independent Emissions Verifiers accredited[26] for the purposes of the CM prior to the Prequalification Window in 2020, so a signature from an Independent Emissions Verifier will not be required until the Prequalification Window in 2021 (see Section A.6.8 below).

- **Reliance on previous Fossil Fuel Emissions Declaration:** A CMU will be able to rely on a previous Fossil Fuel Emissions Declaration when entering the same CMU as part of a future Prequalification application, unless there has been a material change since that Declaration was submitted – i.e. any change to the CMU such that the CMU will contain a Fossil Fuel Component or storage facility connected to a Fossil Fuel Component, or any change to a component comprised in that CMU such that the emissions of that component could be or are altered. In these circumstances, an "updating" Fossil Fuel Emissions Declaration will be required as soon as reasonably practicable after the person becomes aware of the material change. Where the previous Declaration specified compliance with the Fossil Fuel Yearly Emissions Limit, an "updating" Fossil Fuel Emissions Declaration will be required by a date which allows for 12 months of new data to be included in the calculation (see Section A.6.3 below). An updating Fossil Fuel Emissions Declaration will be in the form of Exhibit ZA in the Rules and will indicate the components which have changed.

  Capacity that existed before 4 July 2019 which will exceed the Fossil Fuel Emissions Limit but has declared in an earlier Fossil Fuel Emissions Declaration that it complies with the Fossil Fuel Yearly Emissions Limit will not be able to rely on that Declaration when entering the same CMU in a future Prequalification process even if no material change occurs. A new Fossil Fuel Emissions Declaration, verified by an Independent Verifier, will have to be submitted.

Some respondents flagged that the proposed new reporting and verification mechanism will be introduced close to the Prequalification Window in 2020, and that this might give rise to confusion, due to lack of time to understand and implement the new requirements. We note these concerns. These proposals have been developed to a compressed timeline, after the ACER opinion[27] was published in December 2019, in order to implement Article 22 of the Electricity Regulation in the CM in line with the UK's obligations under EU law. We have been

[23] Defined as *"nominal capacity of a Generating Unit or DSR CMU Component, expressed in MW".*
[24] Fossil Fuel Components (or storage facilities connected to Fossil Fuel Components) with an installed capacity below 1MW will need to make a self-declaration, confirming that that component will not exceed the carbon emission limits (see Section A.6.9 below).
[25] The definition of 'Independent' in Rule 1.2.1 will be amended to include emissions verifiers.
[26] Accredited by the UK's National accreditation body UKAS, or an accreditation body that is a member of the European or international multilateral agreements operated by EA, ILAC and IAF.
[27] As per the requirement in Article 22(4) of the Electricity Regulation, an opinion containing a methodology for calculating the carbon emission limits was published by the Agency for the Cooperation of Energy Regulators (ACER) on 17 December 2019 (the "ACER opinion"). Opinion No. 22/2019 https://www.acer.europa.eu/Official_documents/Acts_of_the_Agency/Opinions/Opinions/ACER%20Opinion%2022-2019%20on%20the%20calculation%20values%20of%20CO2%20emission%20limits.pdf

working closely with the Delivery Body to ensure that any undesired consequences are minimised and we plan to publish a guidance document ahead of the opening of the Prequalification Window in July 2020 to provide further detail about the new requirements.

A.6.2 Unproven DSR, New Build and Refurbishing CMUs

A.6.2.1 Summary of responses

Consultation question 21:

Do you have any views on the proposal that applicants in respect of Unproven DSR will be allowed to declare in their Prequalification applications that they commit to recruiting only components that comply with the emission limits, and to provide an updated declaration as part of the notifying DSR components milestone?

16 respondents addressed Question 21, regarding the proposal that Unproven DSR applicants will be only asked to (a) submit an undertaking not to recruit components above the limits at Prequalification, and (b) provide a full Fossil Fuel Emissions Declaration as part of the Notifying DSR Components milestone.

The large majority agreed with this approach. Those respondents who disagreed expressed a preference for DSR to be treated in the same way as other CMUs, having to confirm components and emissions at Prequalification. One respondent indicated that it would be unfair for DSR to be able to recruit fossil fuel components emitting above the limit, after having prequalified.

Finally, one respondent suggested that DSR should be subject to the same requirements as New Build Generating CMUs and so, after Prequalification, should provide a declaration in the same format as New Build Generating CMUs.

A.6.2.2 Government response

We do not intend to treat Unproven DSR in the same way as Existing Generating or Proven DSR CMUs because, as explained in the consultation, an applicant for an Unproven DSR CMU would not be able to confirm all components that will eventually be recruited at Prequalification. This is a situation which has a parallel in New Build and Refurbishing CMUs at Prequalification, which are also not able to confirm the Installed Capacity and efficiency of their components.

Given the broad support expressed for the measure, we intend to introduce amendments to the Rules to impose similar requirements on Unproven DSR as apply to New Build and Refurbishing CMUs.

Therefore, Unproven DSR, New Build and Refurbishing CMUs will be required to:

- submit a Fossil Fuel Emissions Commitment at Prequalification, which will include a commitment to recruit DSR components or build/refurbish generating units (as the case may be) that comply with the emission limits; and

- submit a Fossil Fuel Emissions Declaration ahead of the following deadlines: For a DSR CMU, this will by the same date that it provides a DSR Test Certificate; for a New Build and Refurbishing CMU, this will be by the deadline for meeting the MCR or the SCM (i.e. the start of the first delivery year or the date the capacity agreement takes effect if the extensions are used).

In respect of a capacity provider which fails to provide a Fossil Fuel Emissions Declaration at the requisite deadline, or provides a Fossil Fuel Emissions Declaration which fails to comply with the Fossil Fuel Emissions Limit (and, if relevant, the Fossil Fuel Yearly Emissions Limit), the termination event in Rule 6.10.1(o) is applicable (due to the declarations made by the capacity provider during Prequalification). In the consultation, we proposed requiring an Unproven DSR to provide a Fossil Fuel Emissions Declaration by the same date it notifies the Delivery Body of its DSR components. However, in order to align more with the requirement in respect of New Build and Refurbishing CMUs and to ensure the Fossil Fuel Emissions Declaration is provided nearer to when a capacity agreement takes effect, we have determined that it is more appropriate for the Fossil Fuel Emissions Declaration to be provided by the same date a DSR Test Certificate is provided. The consultation on Capacity Market Emission limits considered whether the termination event in Rule 6.10.1(o) should have a termination fee attached, and the decision was that it should not. This is considered further at section B.4.2 below.

A.6.3 The Fossil Fuel Yearly Emissions Limit

A.6.3.1 Summary of responses

Consultation question 22:

What are your views on the proposal in section 2.5.4 for requiring reporting for CMUs which seek to take advantage of the yearly limit?

Section 2.5.4 of the Future Improvements Consultation described the Government's intention to require that the yearly limit is calculated on the basis of emissions across the twelve months (one year) before the relevant prequalification window, rather than the average of the three preceding years proposed in the ACER opinion. The twelve months would be those preceding the first day of the relevant Prequalification Window, with the exclusion of any period before 5 July 2019.

14 respondents expressed an opinion on Question 22. The majority of respondents broadly agreed with the proposal, with some flagging their support for the checks to take place before Prequalification, rather than monitoring emissions during the Delivery Year, and for a new Fossil Fuel Emissions Declaration to be submitted every year. A number of respondents qualified their agreement by flagging certain aspects which they wished to see changed, as detailed below.

A small number of respondents disagreed with the proposal, instead suggesting that any participants wishing to take advantage of the yearly limit should only be required to submit a declaration at Prequalification. The main concern driving this preference was that there might be insufficient availability of Independent Emissions Verifiers to certify the calculations of all participants in the first year these changes are introduced.

Some respondents recommended that emissions should be monitored during the Delivery Year, although one suggested, as an alternative, that participants should commit to complying with the emission limits during the Delivery Year.

A number of respondents suggested that the calculation of emissions should be based on the year before the Delivery Year, rather than the year before Prequalification, as this is a more accurate predictor of the emissions during the Delivery Year. Some respondents also noted that having to calculate emissions ahead of Prequalification could impact on their commercial decision regarding operating hours during the year before Prequalification, without any certainty of obtaining a Capacity Agreement.

One respondent suggested that participants should calculate the maximum number of hours they could run within the yearly limit based on an official formula and then self-limit their running hours.

One respondent expressed a preference for compliance to be calculated over three years (as suggested in the ACER opinion) rather than twelve months, as they suggest it would give a more accurate picture of the emissions, as patterns and behaviours can change seasonally and are dependent on outages.

Finally, some respondents flagged a concern about the timing for submitting the Fossil Fuel Emissions Declaration. If the twelve months of data to be analysed ends just as the Prequalification window opens, this would put pressure on any CMUs attempting to prepare and verify their calculations to be included in the Declaration in a short period of time.

A.6.3.2 Government response

In creating the reporting and verification mechanism for the yearly limit, as with the wider mechanism, we strived to strike a balance between ensuring the accuracy and robustness of the reporting mechanism and avoiding an excessive administrative burden for businesses. The fact that the majority of respondents overall agreed with our proposal gives us confidence that we have struck the right balance.

Allowing Existing Generating and Proven DSR CMUs to submit a non-verified declaration at Prequalification would be justified only if it were followed by some form of assurance of the accuracy of the declaration during the relevant delivery year. A monitoring regime would be burdensome for both CM participants and the Delivery Body. Furthermore, we do not believe it would be appropriate to develop a hybrid system which relies on both verification before Prequalification against the Fossil Fuel Emissions Limit and monitoring of emissions during the Capacity Agreement against the Fossil Fuel Yearly Emissions Limit, as this would inevitably add to the complexity of the CM.

Whilst we acknowledge the responses which propose that compliance with the Fossil Fuel Yearly Emissions Limit should relate to emissions data from the year before the first Delivery Year of a capacity agreement, we do not intend to implement this as the proposed mechanism as it would be too complex to implement, requiring the introduction of a new milestone just before the Delivery Year and new termination fees. We do not believe there would be time to consult on the introduction of a new milestone and termination fees in time to meet our legal requirement to apply the emissions limits from the auctions procuring capacity for the Delivery Year 2024/25. Implementing this proposal would also introduce a security of electricity supply risk, as any capacity terminated close to the Delivery Year, for T-4 Agreements, could not be replaced.

With regards to basing the calculation of emissions on the annual average over the three years before Prequalification as opposed to one year before Prequalification (which would align with the recommendation in the ACER opinion), the Government's view is that this would disproportionately constrain the commercial behaviour of plants wishing to generate in excess of the yearly limit in the years prior to deciding to participate in the CM and would therefore be overly onerous for CM participants. Moreover, as noted by respondents, emissions in the twelve months prior to the Prequalification Window are likely to provide a better indication of a CMU's emissions in future as it reflects the commercial behaviour of the CMU closer to the Delivery Year. Furthermore, in the event of a material change, the CMU relying on the yearly limit will need to re-submit a declaration as soon as it has twelve months' worth of data on the CMU after the material change is completed. If the required time period were to be three years, that would mean in most cases the FFED would be submitted well after the relevant Delivery Year.

We acknowledge concerns expressed by respondents relating to the time pressure on CMUs to prepare and verify their Fossil Fuel Emissions Declaration ahead of Prequalification. In order to ease the burden associated with this, we will not proceed with the proposal that the twelve-month period for which emissions data is required, to end at the opening of the Prequalification Window). Instead, the twelve-month period will be required to end at any time during the two full calendar months before the opening of the Prequalification Window.

In order to account for a full twelve months of data to be included in a Fossil Fuel Emissions Declaration made during the Prequalification Window in 2020, and to allow applicants the opportunity to prepare and verify that data, we will not implement the proposal in the consultation which sought to prevent the inclusion of emissions data from before 4 July 2019.

Wider issues about the availability of Independent Emissions Verifiers before the Prequalification Window in 2021 are considered at section 6.8 below.

A.6.4 Monitoring regime

A.6.4.1 Summary of responses

Consultation question 23:

What are your views on the proposal in section 2.5.6 for not establishing a monitoring regime as advised in the ACER opinion?

13 respondents expressed an opinion on the proposal to not establish an in-year monitoring regime of the emissions. The large majority of these expressed support for this approach, which some defined as more pragmatic and cost efficient. Only one respondent expressed opposition to this proposal, arguing that a monitoring regime would be preferable.

A few respondents suggested that any CMUs wishing to prequalify on the basis of the yearly limit, should be required to submit a declaration at Prequalification, and their emissions should be monitored during the Delivery Year. The main reason provided was that timing would be tight for CMUs to gather emissions data, and have that data independently verified, in the twelve months preceding the opening of the Prequalification Window.

A.6.4.2 Government response

In line with the recommendation in the ACER opinion,[28] and the preference expressed by a majority of respondents, we will not introduce a regime which entails monitoring and checks of emissions during a Delivery Year. Rather, we intend to implement a reporting and verification mechanism which is based upon desk-based checks ahead of Prequalification, as described in the Future Improvements Consultation.

The proposal to monitor the emissions of CMUs wishing to prequalify on the basis of the yearly limit is dealt with at Section 6.3.

A.6.5 Waste-to-energy plants

A.6.5.1 Summary of responses

Consultation question 24:

What are your views on the proposal in section 2.5.7 for not applying the emission limits to waste to energy plants?

11 responses were received to Question 24, which sought views on the proposal to exempt waste to energy plants from the emission limits.

The large majority agreed with the proposal. Reasons put forward in support include maintaining consistency with UK legislation (Section 61 of the Energy Act 2013) and consistency with the waste hierarchy approach. One respondent argued that energy-from-waste plants divert non-recyclable waste away from landfill, where it could otherwise give rise to methane emissions over many decades which have a greater global warming potential than carbon dioxide.

Of the small number of respondents that disagreed with the proposal, one argued that the exemption would create a market distortion that could affect competition in the capacity auctions which, from a wider policy perspective, would be inconsistent with the Government reaching its net-zero policy.

A.6.5.2 Government response

In line with the majority view of respondents, we do not intend to amend the definition of a “fossil fuel” in the Rules to include ‘waste’. Generating capacity which is a waste-to-energy plant will, therefore, be out of scope of the CM emission limits (unless any waste falls within paragraph (g) of the definition of “fossil fuel” in Rule 1.2.1).

This measure is consistent with the Government’s net zero ambition, as incentivising waste-to-energy overall reduces emissions that would result from landfill.

[28] ACER opinion No 22/2019 published on 17 December 2019 https://www.acer.europa.eu/Official_documents/Acts_of_the_Agency/Opinions/Opinions/ACER%20Opinion%2022-2019%20on%20the%20calculation%20values%20of%20CO2%20emission%20limits.pdf

A.6.6 Cogeneration (Combined Heat and Power plants)

A.6.6.1 Summary of responses

Although there was no specific question about cogeneration and Combined Heat and Power (CHP) plants in the consultation, 8 respondents commented on the way the reporting and verification mechanism will apply to this form of generation.

The consultation stated, in Section 2.5.9, that '*For cogeneration units such as Combined Heat and Power (CHP) plants, the net electrical efficiency should refer to the generation unit producing only electricity at full load. Where due to the generation unit's configuration production of electricity alone is not possible (e.g. backpressure steam turbines) the heat produced under electricity full load operation mode should not be taken into account*.' This proposal was aligned with the recommendations in the ACER opinion.

One respondent agreed with this approach as it would allow their CHP asset to take part in the CM. However, 7 respondents disagreed with this approach, arguing that it would not be representative of the true efficiency of a CHP plant as heat generated by CHP displaces heat that would have to be generated through a separate and less efficient process, potentially with higher carbon emissions overall. Some of these respondents provided calculations to show that their plants, producing industrial grade heat, would not be able to meet the limits or prequalify, despite having above-average efficiency.

A.6.6.2 Government response

The Government's proposals in the Future Improvements Consultation suggested, at Section 2.5.9, that compliance with the Fossil Fuel Emissions Limit would not be a barrier to CHP generators taking part in the CM. However, in the light of the responses to the consultation, we have refined the emissions calculation as it applies to CHP.

Reflecting upon the responses to the consultation, we believe it would not be appropriate to take account of the production of heat in the emissions calculation as other technologies that produce electricity from fossil fuels also produce heat, albeit as a waste product. Therefore, for heat to be considered in a fair way, we would have to institute some form of monitoring system to check the heat produced as a by-product is actually used and not wasted. As explained at Section 6.4 above, we are not implementing a monitoring system.

However, to ensure that CHP generators are not unfairly excluded from the CM, we intend to introduce an alternative solution. A generating unit that, as part of its electricity generation process produces steam at pressure, will be able to consider its steam output when calculating the efficiency of that generating unit. This will be done by applying an alternative formula when calculating the electrical efficiency of the installation, which takes into account the electricity that could theoretically be generated from the high pressure steam which is produced as part of the generation process and utilised. We will include this formula in the Rules.

We expect this approach will provide emissions calculations which are more reflective of the real efficiency of generating units that produce useful high pressure steam and so ensure they are not unfairly excluded from the CM. We expect that generating units which produce low pressure steam will comply with the emission limits and any otherwise disadvantageous impact our proposed approach will have on this type of plant will therefore not restrict their participation in the CM.

A.6.7 Plants taking part in the EU ETS scheme

A.6.7.1 Summary of responses

Given the current uncertainty surrounding the future carbon pricing policy in the UK, the consultation noted that we do not intend to require or allow CMUs that contain Fossil Fuel Components that are subject to the EU ETS to use the emission factor for CO_2 in the most recent annual EU ETS emission report when calculating their emissions for CM purposes.

6 respondents commented upon this proposal. A number suggested using the EU ETS (and any scheme that might replace it) for the purpose of emissions reporting in the CM, instead of the proposed reporting and verification mechanism. This would be to avoid a duplication of effort and administrative burden for generators who are part of the EU ETS scheme.

Two respondents suggested that it should be possible to use the EU ETS carbon emissions factor when calculating emissions. The main reason given was that it would reduce demand for Independent Emissions Verifiers and therefore help mitigate the risk that there might be insufficient availability of Independent Emissions Verifiers to meet the needs of all applicants in the time available before the Prequalification Window for the next round of CM auctions closes.

Another respondent indicated that, in order to avoid additional operational complexity for capacity providers and the Delivery Body, the reporting and verification mechanism should mirror the cycle of the EU ETS, where the deadline for the submission of reports is 31 March each year, rather than being linked to the CM Delivery Year cycle.

A.6.7.2 Government response

With regards to the suggestion that the reporting of emissions under the EU ETS should be used instead of the proposed reporting and verification scheme, whilst we appreciate that reporting for both may seem like a duplication, reporting under one scheme cannot substitute reporting under the other. Not all participants in the CM are eligible to be part of the EU ETS, and setting up a mixed system where there are two slightly different ways of calculating emissions would fail to create a level playing field as well as being significantly complex to administer. This additional complexity would be further compounded by the misalignment between the EU ETS reporting year and the CM yearly cycle.

Moreover, reliance upon EU ETS reporting would not necessarily reduce the administrative burden on participants in the CM. The proposed reporting mechanism for the CM is designed so that the majority of capacity providers will be able to rely on the same Fossil Fuel Emissions Declaration year after year, unless there is a material change (see section A.6.1.2).

We acknowledge the views of respondents which, in line with the ACER opinion, proposes allowing use of the EU ETS carbon emissions factor when calculating emissions for the purposes of the CM. However, we do not believe that doing so would be an effective mitigation against the risk of insufficient availability of Independent Emissions Verifiers. According to the ACER opinion, if a CMU is unable to use the EU ETS carbon emissions factor, it should use the emissions factor specific to a type of fuel listed in the table at Annex D of the Future Improvements consultation[29], which will form part of the Rules. From an Independent Verifier's point of view, therefore, verification of the emission factor will involve checking against that table, rather than an analysis of the calculations of emission factors under the EU ETS.

[29] An amended version of the table will be included as a new Schedule to the Rules

Furthermore, we anticipate that for the vast majority of CMUs, the emissions calculation in the Fossil Fuel Emissions Declaration (FFED) will only need to be independently verified for the first year.

At the time of the Future Improvements Consultation the Government was not minded to use the EU ETS emissions factor based on a desire to avoid adding complexity to the emissions reporting and verification mechanism (especially given the uncertainty surrounding the future carbon pricing policy in the UK) for what are, at best, very limited advantages which could be enjoyed by only some CM participants. This assessment remains valid in light of the responses received as part of the consultation. Therefore, the Government does not intend to allow the use of the ETS emissions factor in the calculation of emissions for the CM.

A.6.8 Risk of insufficient availability of Independent Emissions Verifiers ahead of the Prequalification Window in 2021

A.6.8.1 Summary of responses

Seven respondents flagged a perceived risk that, with Rule changes expected to be introduced so close to the start of the Prequalification Window for the 2021 CM auctions (due to open in July 2020) there might be insufficient availability of Independent Emissions Verifiers accredited in scope of groups 1(a) and/or 1(b) of Annex I of Regulation (EU) 2018/2067[30] to verify all Fossil Fuel Emissions of CMUs wishing to prequalify. This could produce a bottleneck with some CMUs being unable to secure the required Independent Verification and failing to prequalify as a consequence.

A.6.8.2 Government response

UKAS[31], the UK's National Accreditation Body, will accredit Independent Emissions Verifiers. We estimate there are currently fewer than 10 companies in the UK with the required level of expertise and while we expect these companies to be able to verify more than one Fossil Fuel Emissions Declaration at any one time, we recognise that their availability could come under strain given the short time available to complete verifications in advance of the Prequalification Window in 2020, especially when the time to complete the accreditation process is taken into account. While not all applications for Prequalification will need to include a Fossil Fuel Emissions Declaration, we note that the Delivery Body receives well over 1500 applications in each Prequalification Window. We also note that the issue is likely to be exacerbated by the effects of coronavirus, with generators and Independent Emissions Verifiers experiencing operational delays and difficulties, amongst other things, due to possible staff shortages.

We seek to ensure that Applicants are not unable to prequalify only as a consequence of insufficient availability of Independent Emissions Verifiers, not least as this would potentially produce an artificial increase in the clearing price of the CM auctions and higher costs being passed on to electricity consumers.

In light of this, and as part of a wider attempt to reduce regulatory burden in light of the challenges posed by the effects of coronavirus, the Rules will be amended so that Fossil Fuel

[30] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32018R2067&from=EN. As explained at section A.6.10.5 we intend to remove scope 1a from the qualifying scopes for accreditation.
[31] https://www.ukas.com/

Emissions Declarations made before the Prequalification Window in 2021 (defined as “transitional” Fossil Fuel Emissions Declarations) will not need to be verified by an Independent Emissions Verifier.

It will not be possible to rely on a “transitional” Fossil Fuel Emissions declaration if the same CMU is entered for prequalification for a future auction.

A.6.9 Threshold of 1MW of Installed Capacity

A.6.9.1 Summary of responses

The consultation proposed to apply an exemption (as provided for in the ACER opinion) that a Fossil Fuel Component which is below 1 MW of installed capacity and uses a “commercial standard fuel” is not required to have its emissions calculation verified by an Independent verifier. Instead, applicants would need to make a self-declaration, similar to the one currently contained in the Fossil Fuel Emissions Declaration, confirming that the component would not exceed the carbon emission limits. This was to avoid placing an excessive administrative burden on CMUs which might aggregate a large number of sub-1MW permitted on-site generating units.

Although this proposal was not directly addressed by any specific questions, seven respondents expressed an opinion on it. Some respondents agreed with the proposal, either suggesting it was sensible as it would keep the administrative burden for smaller participants manageable, or agreeing that it would be appropriate to set this threshold at 1 MW given the significant number of plants between 1MW and 5MW already in the CM and the potential for this number to increase.

A number of respondents agreed with the proposal but argued that the threshold should be set at 5MW, as recommended in the ACER opinion. The main reason for this was cost, as respondents argued that the cost of verification would affect smaller participants disproportionately.

Only one respondent disagreed with the proposal, arguing that if units below 1MW are to participate in the CM, then they should be capable of completing the same level of reporting and verification.

A.6.9.2 Government response

The Government does not intend to require verified emissions values for Fossil Fuel Components, and storage facilities connected to Fossil Fuel Components, with an Installed Capacity below 1 MW. Instead, a self-declaration confirming that that component will not exceed the carbon emission limits will be required.

As indicated in the consultation, the proposed threshold of 1MW is lower than the 5MW proposed in the ACER opinion. However, the Government believes it is appropriate for a lower threshold to be set as we are aware that there are a significant number of Fossil Fuel Components in GB with Installed Capacity of between 1MW and 5MW. Ensuring these components are required to verify their carbon emissions calculations will help ensure confidence in the robustness of the mechanism, which is important in the context of the net zero target and given the absence of any ex-post monitoring of emissions. The 1 MW threshold also aligns with the new Minimum Capacity Threshold for entry into the CM.

While we understand that the costs relating to the independent verification could affect smaller participants more than larger plants, this is mitigated by the fact that, for the majority of CM participants, the cost of independent verification would need to be borne only once, as Fossil Fuel Emissions Declarations can be relied on in future years, assuming no material change occurs.

Furthermore, the exemption is mainly aimed at DSR CMUs that might aggregate multiple generators below 1MW which would fall under the Minimum Capacity Threshold for participating in the CM independently and might therefore face multiple costs. For non-aggregated generators, which are able to take part in the CM independently (given the lowering of the Minimum Capacity Threshold to 1 MW), the cost of the independent verification should be factored into the commercial decision to take part in the CM, and we do not believe it would be in itself a barrier to these units taking part.

The proposal outlined in the consultation described a component as being exempt from the verification requirement if it was 'below 1 MW of installed capacity and uses a *commercial standard fuel*.[32] The intent behind specifying the use of commercial standard fuels and excluding the use of fuels such as waste which do not adhere to international fuel standards was, per the ACER opinion, to provide a further level of reassurance with regards to the comparability and reliability of unverified emissions calculations. The Government has decided it will not include in the exemption an additional requirement that the component uses a commercial standard fuel, as it would not provide further reassurance, as emissions from waste-to-energy plants will not be covered by the CM emission limits (as indicated in Section A.6.5 above) and waste would be the main non-standard fuel.

A.6.10 Other changes to the Rules

Upon a detailed review of the Rules, we have identified that minor additional amendments to the Rules will be required to implement some of the emission limits proposals in the Future Improvements Consultation.

A.6.10.1 Eligible Secondary Trading Entrants

In order to take part in secondary trading as an "Acceptable Transferee", the conditions in Rule 9.2.6 must be satisfied. Rule 9.2.6(e) will be amended so that a Fossil Fuel Emissions Declaration will need to be provided to the Delivery Body by a CMU in respect of which a Fossil Fuel Emissions Declaration has not previously been provided.

A.6.10.2 Fuel share

Annex C to the Future Improvements Consultation detailed the formula and parameters for the calculation of the "fuel share" of a generating unit, for use in calculating the emissions of a generating unit which uses more than one fuel. However, as we noted at paragraph 2.5.6 of that consultation, there are currently no generating units participating in the CM using mixed fuels, so the result of the calculation using that formula would always be 100%. Consequently, we will not, at this point, introduce Rules requiring calculation of the 'fuel share' element of the

[32] Defined in Article 3(32) of EU Regulation 2018/2066 to mean *"the internationally standardised commercial fuels that exhibit a 95 % confidence interval of not more than 1 % for their specified calorific value, including gas oil, light fuel oil, gasoline, lamp oil, kerosene, ethane, propane, butane, jet kerosene (jet A1 or jet A), jet gasoline (jet B) and aviation gasoline (AvGas)".*

formula for the calculation of emissions.[33] We will continue to monitor the operation of the CM and review this formula in the future if necessary. This will have no impact on the outcome of the calculation of emissions.

A.6.10.3 Fossil Fuel Removal Declaration

A CMU which, as a consequence of a material change, no longer comprises of a Fossil Fuel Component or storage facility connected to a Fossil Fuel Component will be able to declare this change to the Delivery Body using a "Fossil Fuel Removal Declaration" (a new Exhibit ZC in the Rules).

A.6.10.4 Formulas to calculate emissions of a Generating Unit

In annexes B, C and D to the Future Improvements Consultation, we set out the formulas, taken directly from the ACER opinion, which we proposed would need to be relied upon to determine the emissions of a generating unit. We will introduce a new Schedule 8 in the Rules which will specify these formulas with a number of refinements to clarify and simplify both formulas for ease of application.

"Specific emissions of the generation capacity" (set out in Annex B of the Future Improvements Consultation) and "Fuel share calculation" (set out in Annex C of the Future Improvements Consultation)

The formula for "Specific Emissions" set out in Annex B of the Future Improvements Consultation will be included in a new Schedule 8 in the Rules as the formula for Fossil Fuel Emissions with some refinements. As set out in A.6.10.2 above, the 'fuel share' element is not relevant, and additionally the 'transferred CO_2 factor' element of the formula will also not be included because there are currently no generating units in which CO2 is captured and transferred. We will continue to monitor the operation of the CM and review this formula in the future if necessary.

"Table of Standard Emission Factors of fuels" (set out in Annex D of the Future Improvements Consultation)

We will include this table in a new Schedule 9 to the Rules with some amendments. The values for the fuels that are defined as "fossil fuels" under the definition in Rule 1.2.1 will be included.

In addition, for clarity, we will be expressing the values for $EFCO_2$ in tonnes CO_2/TJ, and the values will be expressed with a full stop instead of a comma as was incorrectly included in the consultation.

A.6.10.5 Scope of accreditation of the Independent Emissions Verifiers

In the Future Improvements Consultation we stated, in line with the ACER Opinion, that the Independent Emissions Verifiers would need to be accredited for the scope of groups 1(a) and/or 1(b) of Annex I of Regulation (EU) 2018/2067. The scopes are described in that Regulation as follows:

[33] This formula will be set out in a new Schedule 8 of the Rules.

1a - Combustion of fuels in installations, where only commercial standard fuels as defined in Commission Implementing Regulation (EU) 2018/2066 are used, or where natural gas is used in category A or B installations.

1b - Combustion of fuels in installations, without restrictions.

Scope 1(a) requires a more limited degree of expertise and capability, so we have determined that it is appropriate to require Independent Emissions Verifiers to be accredited for only the scope in group 1(b). This will ensure the robustness of the emissions verification process for the purposes of the CM. The companies which currently have the required level of accreditation for emissions verification in the UK are accredited for scope 1(b), so there should be enough Independent Emissions Verifiers accredited in advance of the Prequalification Window in 2021.[34]

[34] Fossil Fuel Emissions declarations will not need to be verified by an Independent Emissions Verifier before the Prequalification Window in 2021 – see section 6.8 above.

A.7 Long-term STOR

A.7.1 Summary of responses

Consultation question 26:

Do you agree that it is appropriate to remove the exclusion on Long-term STOR? What would you expect the impacts of removing the exclusion on Long-term STOR to be? Are there any unintended consequences that may arise from removing the exclusion?

21 responses were received in relation to question 26.

A majority of respondents opposed the removal of the exclusion on Long Term STOR ("LT STOR") contract holders competing in the CM. These respondents generally felt the removal would lead to market distortions and windfall profits for LT STOR contract holders. Several respondents also felt the justification for removing the exclusion was not sufficient.

A number of respondents noted that LT STOR contract holders often use diesel generation units, and they believed such units would not be able to pass the new emission limits in the CM, so the removal would be unlikely to create long term issues. One respondent stated that removing the exclusion would encourage more fossil-fuel generation to enter the CM which would be at odds with the Government's net-zero ambitions.

Numerous respondents thought that LT STOR contract holders had made the business decision to opt for LT STOR contracts over competing in the CM. The revenues received by LT STOR contract holders was regularly referenced by respondents, with a number challenging whether there would be a reduced risk of windfall profits from allowing LT STOR contract holders to access the CM now, as compared to in 2014. Several respondent noted that, although utilisation of LT STOR had been limited in recent years due to the higher utilisation prices for LT STOR relative to other types of STOR, recent changes to STOR mean that LT STOR contract holders could now vary their utilisation prices. This may allow them to compete with other STOR providers and thus make more revenue from utilisation. One respondent also noted that LT STOR receive availability payments in addition to utilisation payments. They presented analysis showing LT STOR availability payments as being comparable to other balancing service contracts, but the respondent noted the challenges in making such comparisons, highlighting that other balancing service providers typically have to revenue stack in order to receive comparable payments, and that these revenues are not guaranteed over a long period in the same way that LT STOR is.

Several respondents supported revoking the exclusion. One respondent in favour noted that changes to the STOR market in recent years had created operational challenges which had lowered revenues from STOR. Analysis commissioned by the respondent showed the rate of capital return in relation to projects with a LT STOR contract may be lower than comparable projects with a CM agreement. The respondent also noted that the overall impact of revoking the restriction would be negligible because the LT STOR contract holders make up a very small proportion of GB's capacity and the contracts will all expire in 2025 (and are no longer being awarded by National Grid). Another respondent in favour of the change felt the impact would be largely self-balancing as it would allow some capacity to compete that had not previously and so might increase the liquidity of the capacity auctions. Similarly, one

respondent noted their belief that it is in the consumers' interest that all capacity capable of providing security of supply during system stress should be eligible for the CM, particularly when the market conditions for LT STOR contract holders have changed significantly.

Several respondents questioned how LT STOR exclusions would interact with the forthcoming participation of cross-border capacity in the CM. One respondent felt that, if the exclusion of LT STOR contracts continued, the Government would have to check the balancing service contracts held by foreign plants competing in the CM and apply a similar exclusion, in the interests of fairness.

A.7.2 Government response

The exclusion of capacity with LT STOR contracts from the CM was made in 2014 as it was believed, at that time, that allowing plants with these contracts to compete in the CM would result in windfall profits as they were expected to yield very high revenues. The exclusion was therefore put in place to ensure compliance with the Guidelines on State aid for environmental protection and energy (EEAG),[35] which states in paragraph 230 that the measure [the Capacity Market] *should have built-in mechanisms to ensure that windfall profits cannot arise.*

Since 2014, the energy landscape has changed significantly, and the LT STOR contracts have not yielded the very high revenues that they were originally expected to. Revenue from LT STOR contracts is now similar to revenue from other balancing and ancillary services, none of which are excluded from the CM. Some ancillary services also offer long-term contracts (e.g. Black Start). We have therefore decided to remove the exclusion, as it can no longer be justified as necessary in order to meet the EEAG (paragraph 230).

Regarding the fact that the decision to enter the LT STOR contracts was made before the CM was implemented, this alone is not a sufficient justification for maintaining the exclusion, as it does not necessarily result in windfall profits. We note that there is plenty of capacity in the CM which was financed and built without the consideration of CM revenues.

Respondents suggested some LT STOR contract holders would be unable to compete in the CM because their portfolios often contain diesel generation units which would exceed the emission limits in the CM. We agree that the emission limits may prevent some LT STOR contract holders from entering the CM. However, we cannot rule out the possibility that some of the capacity with LT STOR contracts could be eligible to compete in the CM. Therefore, we do not believe this provides sufficient justification for maintaining the exclusion.

The Government recognises the points raised by respondents on revenue stacking and foreign participation. Cross-border capacity participation will be implemented after LT STOR contracts have expired. It is also beyond the scope of this consultation, but we intend to publish a call for evidence on cross-border participation in due course, and we have noted the helpful feedback provided by respondents.

To remove the exclusion, Regulation 18 will be revoked. Corresponding changes will also be made to Regulations 15 and 19 to remove references to Regulation 18. References to Regulation 18 will be removed from the definition of Mandatory CMU in Rule 1.2.1 and the definition of Relevant STOR contract will be removed from Rule 1.2.1.

[35] Paragraph 230: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52014XC0628%2801%29

A.8 Fraud and Error

A.8.1 Summary of responses

Consultation question 27:

Do you agree with our proposals to require additional information to be added to the CM Register? Do you agree this will advance our fraud and error objectives? If not, can you please provide reasons?

Consultation question 28:

Do you agree with our proposal to require that the same information requirements should apply to Capacity Providers who already hold Capacity Agreements?

The 16 responses to Question 27 were split between support for and opposition to our proposal. The most common reason given for disagreeing with this proposal was the increased administrative burden it would place on Capacity Providers to submit and then keep up to date, the name and addresses of two directors.

From the responses submitted, it is evident that it is not widely known that the Delivery Body and the Settlement Body have limitations on the extent to which they can share data. One respondent who was aware of these limitations, suggested that a better way forward would be to allow greater data sharing between the Delivery Body and Settlement Body.

A small number of respondents noted that, whilst they disagreed with the proposal to add directors' data to the register, they would support agents' details being recorded and maintained.

In response to Question 28, the 15 responses were again split between those who disagreed with our proposal and those who agreed. A small number of those that had disagreed with our proposal in relation to Question 27 suggested that, if we were to adopt the recording of directors' names and address, then it should apply retrospectively to all Capacity Providers.

A.8.2 Government response

The Government acknowledges that opinion was split on whether to add two directors' names and addresses to the CM register and, if so, to make this requirement apply for existing capacity providers.

Reducing the scope for fraud and error within the CM remains an important objective of the Government. However, we intend to carry out further investigation and stakeholder engagement before introducing any changes. We will consider fraud and error again in due course and, if necessary, will consult on updated proposals.

Rules so that Refurbishing CMUs that exceeded the emission limits would be only eligible for 1-year agreements in those auctions.

- How best to deal with false or inaccurate Fossil Fuel Emissions Declarations and the recovery of Capacity Payments in such cases. The Rules already establish arrangements for terminating Capacity Agreements and recovering Capacity Payments in circumstances in which Capacity Providers have made false or inaccurate declarations. Views were sought on whether it is necessary to amend these existing arrangements in respect of the Fossil Fuel Emissions Declarations, including whether a termination fee should be introduced and if so at what level.

Subsequent to the Government's consultation closing, and as per the requirement in Article 22(4) of the Electricity Regulation, an opinion containing a methodology for calculating the carbon emission limits has been published by the Agency for the Cooperation of Energy Regulators (ACER) on 17 December 2019 (the "ACER opinion").[41] Building on the ACER opinion, the Government consulted on further changes to the Rules to implement arrangements for reporting emissions and verifying the carbon emission limits. This was the subject the "Future Improvements Consultation, and the Government Response to this consultation is provided in Section A.6.

B.1.2 Summary of responses to the Summer 2019 consultation

In total, 24 responses were received from a range of stakeholders, including Capacity Providers, system operators and trade associations.

Generally, the majority of respondents were supportive of the Government's proposals. Most of the respondents agreed with the Government's proposal to align the entry into force of the CM emission limits with the Delivery Year, by applying the limits from 1 October 2024. A minority expressed a concern for security of electricity supply connected to this date.

Just over half of the respondents agreed that Refurbishing CMUs that will exceed the emission limits should only be eligible for 1-year agreements. The remaining respondents were split amongst those who considered that the capacity agreement should be awarded for the usual 3 years length, and those who argued that agreements should not be awarded at all if Refurbishing CMUs are expected to exceed the emission limits.

The picture on the issue of termination fees and arrangements for repayment of capacity revenues in the event of a false or inaccurate Fossil Fuels Emissions Declarations was less clear cut. Around half of the respondents expressed a preference for termination fees to be based upon one of the existing fee rates which are listed in the Regulations. However, there was no consensus as to which termination fee rate. Just under a third of respondents indicated that the fee rate should be set at a high enough level so that it would not be priced into auction bids and would act as a deterrent against non-compliance.

Amongst the five respondents who indicated a preferred termination fee rate, TF3 (£10,000/MW) was the one that was preferred by the largest minority. Around a third of

[41] Opinion No. 22/2019
https://www.acer.europa.eu/Official_documents/Acts_of_the_Agency/Opinions/Opinions/ACER%20Opinion%2022-2019%20on%20the%20calculation%20values%20of%20CO2%20emission%20limits.pdf

B.2. Implementation date for emission limits for capacity existing before 4 July 2019

B.2.1 Summary of responses

Consultation Question 1:

Should the emission limits for existing generation be implemented as of 1 October 2024 or 1 July 2025? What would be the potential impact of the two options on existing generation capacity?[42]

Consultation Question 2:

If you believe the 1 July 2025 date to be preferable, which sub-option do you prefer?

Sub option 1 - only until 1 July 2025, after which time the agreements will be automatically terminated; or

Sub option 2 - for the full 2024/25 Delivery Year until 30 September 2025, but will only be eligible for payments until 1 July 2025.

A significant majority of the 22 respondents to Question 1 indicated a preference for the emission limits being implemented from 1 October 2024. The main reason given for this preference was that aligning the implementation date with the start of the CM year would be simpler and would avoid the need to create further ad hoc regulation, therefore providing more certainty to the market and potentially avoiding additional administrative burdens for CM participants.

Another reason given for a preference for 1 October 2024 was that bringing the deadline forward would reduce overall emissions and therefore better align with the UK's ambitions on tackling climate change.

Some respondents caveated their preference for a 1 October 2024 application date indicating that it was predicated on this not causing security of electricity supply concerns.

Two respondents noted that preventing coal generators from taking part in the CM from 2024 might in practice mean that coal plants are forced to close, due to adverse economics, when the limits are introduced. One respondent flagged this could create a misalignment between this and the Government's commitment to regulate for the closure of unabated coal generation by 1 October 2025.

A small minority of respondents indicated a preference for the limits to apply from 1 July 2025, due to perceived risks to security of supply if unabated coal generation, and possibly a small amount of OCGT and reciprocating engines, were not able to take part at all in CM auctions for the Delivery Year 2024/25. In particular it was noted that a misalignment in dates between the Government's policies on regulating for the closure of coal and applying emission limits in the

[42] The references to "existing capacity" in this consultation means capacity existing before 4 July 2019.

CM would effectively remove the Secretary of State's emergency power to suspend the regulation for the closure of coal, where there might be a shortfall in electricity generation, no earlier than six months before 1 October 2025.

Due to the majority preference to apply the limits from October 2024, only seven respondents engaged with Question 2 which looked at the two possible sub options for implementing the emission limits from July 2025. Support for the two sub options was almost equally split. Respondents who expressed a preference for sub option 1 indicated that it would be unfair for Capacity Providers above the limits to be paid for nine months but face liability for non-delivery for the whole duration of the contract. Respondents who indicated a preference for sub option 2 expressed a concern for security of supply as the reason for this.

B.2.2 Government response

The Prime Minister announced, on 4 February 2020, an intention to publish a consultation seeking views on bringing forward deadline for phasing out unabated coal phase to 1 October 2024. The Government notes that, if coal generation were to be allowed to prequalify for the auctions and bid for capacity agreements for even part of the Delivery Year 2024/25, a subsequent decision to close unabated coal from 1 October 2024 could lead to a gap in capacity for that Delivery Year, as any capacity agreements awarded to coal generators would have to be revoked. To avoid any security of supply risks that this would create, the Government intends that emission limits for existing capacity will be implemented in the CM as of 1 October 2024.

As noted by respondents to the Summer 2019 Consultation, applying the CM emission limits from 1 October 2024 is also better aligned with our commitment to net zero as it is important to go further and faster wherever possible. Applying the limits from this date will also enable us to demonstrate international leadership in this area, building on our leadership of the Powering Past Coal Alliance, which has attracted significant global attention, and providing important signalling ahead of COP26 (which has been postponed due to the effects of coronavirus) where emissions from the power sector is likely to be a key issue.

A full impact assessment will be published alongside the planned consultation on bringing forward the unabated coal phase out deadline to 1 October 2024. In summary, given we expect only a small amount of unabated coal generation capacity, as well as a negligible amount of other capacity with high carbon emissions, to be operating beyond 1 October 2024 in the absence of Government intervention, the impact of this small amount of capacity not being available to secure agreements in the capacity auctions for the 2024/25 Delivery Year should be manageable given the ability to secure alternative capacity. We are, therefore, confident that applying the CM emission limits from 1 October 2024 will not adversely affect our security of electricity supply. Similarly, our assessment of the impact on consumer bills is that this should also be minimal. See Annex 2.2 for a summary of expected impacts.

The Government's view is that applying the CM emission limits at the start of the 2024/25 Delivery Year, rather than part way through the Delivery Year, avoids creating administrative burdens and regulatory complexity which stakeholders have expressed is undesirable:

- In the case of sub-option 1 (i.e. agreements for CMUs above the emission limits are automatically terminated on 5 July 2025) this would potentially require the Government

B.4. Termination fees, the recovery of payments, and arrangements for CMUs that exceed emission limits

B.4.1 Summary of responses

Consultation question 4:

What termination fee level should apply to the termination event where a false declaration has been made, or where capacity fails to meet the relevant emission limits?

Consultation Question 5:

In the event of termination, should payments be repaid from the beginning of the Capacity Agreement, or from the date that the CMU fails to meet the emission limits?

Around half of the 19 respondents to Question 4 expressed a preference for termination fees to be set by reference to one of the existing termination fee rates which are listed in the Regulations. However, there was no consensus as to which termination fee rate should be utilised. Just under half of the respondents indicated that fees should be set at a high enough level to act as a deterrent against non-compliance, but in most cases no specific level of fees was indicated.

Amongst the few respondents who indicated a specific termination fee rate, TF3 (£10,000/MW) was the one that was preferred by the largest minority. Around a third of respondents expressed support for a principle where higher termination fee rates are applied to wilfully false declarations and lower termination fee rates are applied to administrative errors.

On the issue of repaying Capacity Payments following termination, a majority of the 17 respondents to Question 5 indicated this should occur from the date the CMU fails to meet the emission limits (TP2). A minority indicated that repayments from the start of the CM agreement (TP3) should be preferred as this would act as a stronger deterrent against making inaccurate or false declarations.

A number of respondents requested clarification on the methodology for calculating compliance with the emission limits and on how compliance would be monitored. One of the issues flagged was that the Electricity Regulation indicates that emission limits should be calculated based upon design efficiency rather than real world measurements. A few respondents also asked for clarification on how the yearly allowance (350kg CO2/installed kW) contained in Article 22(4)(b) of the Electricity Regulation will be monitored and enforced.

One respondent suggested that the UK Environmental Regulatory authorities (Environment Agency, Scottish Environment Protection Agency, Natural Resources Wales, Northern Ireland Environment Agency) already regulate plants that are restricted in operational hours due to their environmental performance, and suggested using this information to avoid adding further reporting burden on generators.

SECTION C: Government Response to the Consultation on Capacity Market easements in light of the coronavirus

C.1. Introduction

The Government's strategic response to the coronavirus pandemic is STAY ALERT, CONTROL THE VIRUS, SAVE LIVES. The pandemic and measures being taken to delay its spread are likely to impact holders of Capacity Agreements, including their ability to achieve compliance with the obligations to the set deadlines in some instances. This is in addition to the effects of the recent standstill period still being felt by some Capacity Providers.

The Government, therefore, considered ways to reduce burdens on Capacity Providers as they focus on dealing with the impact of coronavirus on their business. The objective was to minimise, as far as possible, the risk of terminating and imposing termination fees on CMUs that fail to meet an obligation as a result of the effects of coronavirus.

The easements we intend to put in place will be applied in a time-limited manner in the legislation, such that they are only applicable to certain capacity providers, CMUs or CM participants and/or expire after a certain period. We will keep the need for further easements under review and may come forward with proposals in due course, if necessary.

C.1.1 Summary of consultation proposals

The Government ran a consultation from 24 to 30 April 2020 (the "Easements 2020 Consultation") which sought views on proposals to temporarily modify the application of the Regulations and the Rules to:

- Prevent the suspension of Capacity Payments if a CMU with an agreement awarded in an auction held after 21 December 2017 fails to demonstrate three separate SPDs during the 2019/20 winter.

- Extend the deadline for Metering Tests for certain CMUs holding T-1 agreements for Delivery Year 2020/21.

- Extend the Long-stop Date for both New Build CMUs awarded T-1 agreements for the Delivery Year 2020/21 and Refurbishing CMUs with multi-year agreements which start in Delivery Year 2020/21, by twelve-months.

- Remove the requirement for an ITE report in relation to any Six Monthly Progress Reports falling due during the 2020/21 financial year for New Build CMUs and Refurbishing CMUs.

C.2. General Easements

C.2.1 Satisfactory Performance Days

Consultation proposal:

Prevent suspension of Capacity Payments if a Capacity Market Unit (CMU) with an agreement awarded in an auction held after 21 December 2017 fails to demonstrate three separate SPDs during the 2019/20 winter.

C.2.1.1 Summary of responses

Five respondents identified an ambiguity in the proposal and clarified that agreements awarded in auctions held before 21 December 2017 also face suspension of payments if they fail to demonstrate Satisfactory Performance Days (SPDs) by 30 April. A number of respondents also queried how the Government would ensure the suspension of Capacity Payments did not affect Capacity Payments for May given the proposed amending legislation would be unlikely to be in place until later. Some suggested that the Government should apply any provisions in this regard on a retrospective basis.

Of the 12 respondents who expressed an opinion on this proposal, the large majority supported payments not being suspended. One respondent did not agree with this proposal and maintained payments should still be suspended. All respondents who expressed an opinion stated that the removal of the suspension should apply to all agreements, not just agreements awarded on or after 21 December 2017.

One respondent suggested that CMUs with agreements issued after 21 December 2017 and that had failed to demonstrate its SPDs by 30 April should have the window for demonstrating additional SPDs extended from 31 July until the end of the Delivery Year.

One respondent suggested that, in order to not have payments suspended, Capacity Providers should demonstrate the failure to meet SPDs was a direct result of the coronavirus pandemic supported by an ITE report.

C.2.1.2 Government response

The Government welcomes the comments submitted in relation to this proposal and, in line with the view of the majority of respondents, intends to proceed with its implementation.

The Government wishes to clarify that, as noted by respondents, agreements awarded in auctions held before 21 December 2017 also face suspension of payments if they fail to demonstrate their SPDs by 30 April. To ensure easements are afforded equitably to these different groups of Capacity Agreements, the Government confirms that implementation of this proposal will apply to all agreements awarded to date and which are subject to satisfactory performance requirements in Delivery Year 2019/20.

To enable the easement to apply to Capacity Payments that would otherwise be suspended in May 2020, the Government intends to modify the application of the Regulations and the Rules to enable back payments to be made to those CMUs that did not successfully demonstrate

SPDs over the winter but are successful in meeting their satisfactory performance requirements in the timeframe allowed to them under the Rules. Specifically:

- For pre 21 December 2017 agreements, providers will be paid any suspended payments if the CMU meets its SPD requirements by 30 September 2020; and

- For agreements awarded on or after 21 December 2017, providers will be paid any suspended payments if the CMU demonstrates the three additional SPDs required by the Rules by 31 July 2020.

- The Settlement Body will make back payments once a CMU fulfils its satisfactory performance requirements.

The Government is not minded to extend the time that CMUs with agreements awarded on or after 21 December 2017 have to demonstrate any additional SPDs. The deadline will remain 31 July 2020 as we feel this provides sufficient time for the small number of Capacity Providers likely to be affected to meet their satisfactory performance requirements. We also note that CMUs that receive a termination notice for failing to meet satisfactory performance requirements may appeal to the Secretary of State to request an extension of the date specified in a termination notice to comply if they believe this is merited by their individual circumstances.

We do not intend to require CMUs to provide evidence, verified by an ITE, that the failure to meet SPDs was due to the effects of coronavirus as we feel the administrative burden would be disproportionate to the benefits to the Capacity Provider.

C.2.2 Metering Tests

Consultation proposal:

To extend the deadline from 17 September to 30 September 2020 for the following CMUs holding T-1 agreements for capacity obligations which begin to have effect in Delivery Year 2020/21: Existing CMUs (including any Pre-Refurbishing CMUs treated as Existing CMUs), Proven DSR CMUs and Unproven DSR CMUs.

C.2.2.1 Summary of responses

All thirteen respondents commenting on this proposal expressed support. A small number wanted the Government to go further. Three respondents requested that this deadline be extended to agreements awarded in the T-4 auction for the 2020/21 Delivery Year. One respondent asked if the metering test deadline could be delayed beyond the start of the Delivery Year. A further respondent requested that metering tests be allowed during the Prequalification period.

C.2.2.2 Government response

The Government is minded to implement the changes outlined in the consultation, namely that we will extend the deadline for submitting Metering Test certificates from 17 September to 30 September 2020 for the following CMUs holding T-1 agreements for capacity obligations which

begin to have effect in Delivery Year 2020/21: Existing CMUs (including any Pre-Refurbishing CMUs treated as Existing CMUs), Proven DSR CMUs and Unproven DSR CMUs.

We are not minded to extend the date for metering tests beyond the 30 September and into the Delivery Year as we feel that any benefits arising to Capacity Providers from that change would not be proportionate to the increased risk to security of supply. We also note that CMUs that receive a termination notice for failing to meet Metering Test requirements may appeal to the Secretary of State to request an extension of the date specified in a termination notice to comply if they believe this is merited by their individual circumstances.

The Government is not proposing to make any amendments in relation to the Metering Test deadline applicable to agreements acquired in the T-4 auction for the 2020/21 Delivery Year as this falls 21 months prior to the start of the first Delivery Year and has already passed.

C.2.3 Long-stop Date

C.2.3.1 Summary of responses

Consultation proposal:

To extend the Long-stop Date for both New Build CMUs awarded T-1 agreements for the Delivery Year 2020/21 and Refurbishing CMUs with multi-year agreements which start in Delivery Year 2020/21, by 12-months. Capacity Payments will not be made until the relevant milestone is met (the SCM or MCR). In order to qualify for the extension, an ITE report would need to be provided to the Delivery Body by 1 October 2020, confirming that the project would have met its SCM by October 2020 had it not been for the impacts of the coronavirus.

Respondents were generally in favour of introducing an extended Long-stop Date. Several respondents felt that the extension should be expanded to include other types of CMU potentially impacted by the effects of the pandemic, such as:

- All New Build CMUs that are currently under construction;
- CMUs that won agreements in the T-3 and T-4 auctions held in early 2020, as these CMUs may already have faced delays due to the State aid standstill period (between November 2018 and October 2019); and/or
- New Build CMUs with agreements that were due to commence in Delivery Year 2019/20 but are working towards a Long-stop Date of 30 September 2020 as they experienced delays following last year's the State aid standstill period and are now facing further delays due to the pandemic.

Of those who disagreed with the proposed extension, two respondents thought that an extension of six months, rather than one year, would be sufficient for New Build CMUs given Capacity Providers also have the ability to appeal against termination and seek additional time to meet the SCM. One respondent thought that the extension was not necessary at all, for the same reason. They highlighted the importance of ensuring the CM continues to provide strong incentives for New Build capacity to be brought forward.

Several respondents suggested making changes to ensure Refurbishing CMUs that miss their Long-stop Date of 30 September 2020 do not revert to a one-year agreement.

A few stakeholders requested clarification on when Capacity Payments should commence if the extended Long-stop Date was utilised, particularly for Refurbishing CMUs that are eligible for the extended Long-stop Date, and what sanctions there would be for a delay in achieving the new milestones, including whether CMUs that failed to meet the extended Long-stop Date would be excluded from entering future auctions.

Respondents were generally in favour of an ITE report being required in order to qualify for the extended Long-stop Date. Several respondents thought the ITE should only assess whether the CMU was on track to meet its deadlines up until the time the pandemic began (also suggesting that the date the World Health Organisation announced the pandemic – 12 March 2020 – would be a suitable date to use for the start of the pandemic) as it would not be possible for the ITE to assess whether the SCM would have been met by the CMU by 30 September 2020 if the pandemic had not have happened. One respondent thought that if the ITE could justify delays as being caused by the effects of coronavirus, then these should be allowed to be included within the assessment, even if they occurred before 12 March 2020.

One respondent wanted an extra month to provide the report, to allow projects likely to be close to the original deadline to focus their efforts into completing their projects by 1 October as planned. Another respondent queried whether, if an ITE report is submitted early, a further report would be required to verify it remains accurate at the start of the Delivery Year.

A few respondents pointed out that consequential changes will be needed to the following requirements, to maintain alignment with the extended Long-stop Date for prospective generating CMUs:

- The relevant windows of time in the definition of total project spend (77 months for New Build CMUs and the auction results day for Refurbishing CMUs);
- The deadline for providing an ITE certificate to the Delivery Body confirming that the extended years criteria has been met; and
- The deadline for providing an ITE certificate to the Delivery Body confirming the total project spend.

C.2.3.2 Government response

In line with the majority view of respondents, the Government intends to extend by 12-months the Long-stop Date for: New Build CMUs awarded T-1 agreements which start in Delivery Year 2020/21; New Build CMUs awarded T-4 agreements which were due to start in Delivery Year 2019/20 (i.e. currently have a Long-stop Date of 30 September 2020); and Refurbishing CMUs with multi-year agreements which start in Delivery Year 2020/21.

We recognise there are additional Prospective Generating CMUs which hold obligations for the Delivery Year 2020/21 and whose construction may be delayed by the pandemic, beyond those identified in the consultation. In particular, New Build CMUs that were awarded agreements in the 2015 T-4 and are not on track to meet their Long-stop Date, due to delays resulting first from last year's standstill period and now the effects of coronavirus. We agree that these CMUs should also be able to extend their Long-stop Date by 12 months, until the start of the 2021/22 Delivery Year and will include these CMUs within the scope of the extension.

Whilst we are making changes to the appeals process to increase the time the Secretary of State can grant as an extension before an agreement is terminated to enable Capacity Providers to comply with requirements (see Section C.4), we understand that termination notices can have significant consequences for Capacity Providers e.g. covenants in financial agreements can be triggered by termination notices. It is, therefore, preferable to proceed with implementing the extended Long-stop Date rather than solely relying on Capacity Providers availing themselves of the appeals process. Even with the extended Long-stop Date, there is sufficient incentive for Capacity Providers to deliver as soon as possible, as Capacity Payments don't begin until the capacity is delivered and the SCM is met and there will be other, broader financial consequences for the CMU in the event of late delivery (e.g. missed opportunity to earn revenues in other markets, ongoing development costs).

Regarding whether CMUs that are terminated for failing to meet the SCM by the extended Long-stop Date will be excluded from future auctions, we will not be making any changes to the declaration a Prequalification applicant must make under Rule 3.3.3(f) that the application is for a New Build CMU that has not been terminated in the past two years under certain termination events (which includes termination for failing to meet the MCR – covered in Rule 6.10.1(c)).

Whilst we understand the pandemic may have caused delays for Prospective Generating CMUs which have agreements for Delivery Years later than Delivery Year 2020/21 and are currently under construction, we are not at this time implementing an extension in relation to these CMUs. These CMUs have a longer delivery timeframe which affords the potential for them to catch-up any delays caused by the effects of the pandemic once it is over. That said, we will monitor the need for further extensions and may makes changes in relation to future Delivery Years if necessary.

In line with the majority view of respondents, we will require an ITE report to be submitted by all CMUs that wish to qualify for the extended Long-stop Date. We agree with respondents that it would not be reasonable to ask ITEs to confirm that the deadline for the SCM would have been met if the pandemic had not happened. We will, therefore, only require that the ITE report confirms the CMU was on track to meet the deadline for the SCM when the pandemic began. We will define the start date of the pandemic as 12 March 2020, in line with the announcement by the World Health Organisation. Only one ITE report will need to be submitted, even if it is submitted ahead of the start of the Delivery Year. The deadline for submitting the ITE report will be 30 September 2020, the last day before the start of the Delivery Year.

The extended Long-stop Date will be implemented through changes to the definition of the Long-stop Date in Rule 1.2 to refer, where a CMU meets certain eligibility requirements, to the Extended Long-stop Date (a new defined term). The Rules will be modified to insert a new Rule 6.7.4A setting out the eligibility requirements for a New Build CMU or a Refurbishing CMU to qualify for the Extended Long-stop Date, including the requirements for the ITE report. Capacity Payments for eligible CMUs will only begin once the SCM or MCR has been met, and we will amend Rule 6.7.4(a)(ii) to enact this.

We welcome comments from respondents which highlight additional changes to the Regulations and Rules that are needed to enact the extended Long-stop Date. We agree with respondents that we will need to make changes in the follow areas:

- the expenditure windows in the definition of Total Project Spend,

- the deadline for the ITE report on the Evidence of Total Project Spend, and
- the deadline for the ITE report on the Extended Years Criteria.

To enact these, we will amend Rule 1.2 (definition of Total Project Spend), Rule 8.3.6 (Evidence of Total Project Spend) and Rule 8.3.6A (Meeting the Extended Years Criteria).

For the change to the definition of Total Project Spend and the Extended Years Criteria, we will modify the definition of the expenditure windows for all New Build and Refurbishing CMUs so that if the Long-stop Date or the extended Long-stop Date is utilised, the spending window closes when the SCM or MCR has been met, rather than at the start of the first Delivery Year of the agreement.

C.2.4 Independent Technical Expert Reports

C.2.4.1 Summary of responses

Consultation proposal:

To remove the requirement for an ITE report in relation to any Six Monthly Progress Reports falling due during the 2020/21 financial year for New Build CMUs and Refurbishing CMUs (i.e. from 1 April 2020). The requirements for an ITE Report on Operational Status for Distribution Connected sites and Refurbishing CMUs will be maintained.

The large majority of respondents were in favour of removing the requirement for ITE reports to accompany the six-monthly progress reports. Many suggested that these reports were not particularly helpful in providing assurance to the Delivery Body and referred to Ofgem's Five-year Review of the Rules, which proposed removing ITE reports from the six-monthly progress reports under certain circumstances. One stakeholder recommended that it be clearly communicated to capacity providers that six-monthly reports are still required within the 2020/21 financial year, and it is only the requirement for the ITE report that will be removed.

The majority of respondents were content that the requirement for the ITE report on the operational status of Distribution and Refurbishing CMUs should be maintained and agreed that these could be completed without a site visit. One respondent noted that this could result in a reduction in quality of the reports. Two respondents thought that, if a director's declaration were required rather an the ITE report, then the deadline for the delayed ITE report should be September 2021 rather than April 2021. One respondent was unclear which requirements for ITE reports we were considering waiving due to the wording of the proposal that these requirements should be waived "where these might be impossible or very difficult to obtain due to the need for ITEs to access the sites to prepare such reports".

One respondent noted that, where a progress report identifies that a CMU will miss its SCM by the start of the Delivery Year, Rule 12.2.4 requires a remedial plan to be accompanied by an ITE report. They claimed this requirement could undermine the effectiveness of the proposal to waive the ITE report associated with a progress report, especially where delayed projects need to submit an ITE project in order to be eligible for the extended long stop date. Another respondent noted that Capacity Providers would struggle, due to the effects of coronavirus, to meet the objective of the remedial plan which is to show how the CMU's construction

C.3 Demand Side Response Easements

C.3.1 Metering Assessment, Metering Test and DSR Test Deadline

C.3.1.1 Summary of responses

Consultation proposal:

To give DSR aggregators with Unproven DSR CMUs holding T-1 or T-4 agreements for capacity obligations which begin to have effect in the 2020/21 Delivery Year an additional 12 months to comply with these requirements.

Most respondents either supported or did not comment on the proposed easements relating to the testing requirements for DSR.

A small number of respondents opposed the easements on the basis that Capacity Providers for DSR CMUs can already mitigate their exposure to non-delivery risks by engaging in secondary trading ahead of their DSR test. Some respondents suggested we go further and enable DSR to engage in a form of staged commissioning in a manner similar to the MCR available to Generating CMUs. These respondents suggested that, if a percentage (e.g. 90%) of the DSR capacity could be delivered on time and an ITE provided a report stating the delay to the remainder of the capacity was due to the effects of coronavirus, then an extension should be granted to allow the delivery of the remaining capacity at a later point in the Delivery Year.

A small number of respondents felt that the requirement to provide an ITE report was unnecessary.

One operator questioned whether the extensions would apply if the CMU acquired a capacity obligation through secondary trading from an Unproven DSR CMU.

C.3.1.2 Government response

Whilst the Government recognises that Unproven DSR CMUs already benefit from some flexibilities in relation to the delivery of capacity by the start of the Delivery Year, we believe that giving DSR providers an additional 12 months to comply with the Metering Assessment, Metering Test and DSR Test requirements is proportionate to the issues and difficulties faced by DSR providers due to the effects of coronavirus. We also feel that this will help maintain consistency with arrangements being introduced for Generating CMUs.

The Government is not minded to introduce staged commissioning as suggested by some respondents, as this would provide greater flexibility than afforded to generating CMUs (which only become eligible to receive Capacity Payments once their SCM or its MCR is met). Additionally, and as noted by other respondents, Unproven DSR CMUs already benefit from some flexibilities in relation to the delivery of capacity by the start of the Delivery Year.

With respect to the ITE reports, this is necessary to provide reassurance that the extended deadlines are only being utilised where delays are caused by the effects of coronavirus and to ensure consistency with the arrangements being introduced for generating CMUs.

Operators that are increasing their capacity obligation through secondary trading for Delivery Year 2020/21 should be prepared to deliver this capacity in time for the start of this Delivery Year, including completing associated metering (noting that there is a two week extension for the metering test for certain CMUs with an agreement that starts in Delivery Year 2020/21 – see Section C.2.2). If the transferor of the capacity obligation is an Unproven DSR CMU, this does not necessarily mean that the extensions for Unproven DSR CMUs to the metering assessment, metering test and DSR Test will apply to the transferee; this will depend on the CMU type of the transferee.

C.3.2 DSR Baseline Demand

Consultation proposal:

To shorten the period for establishing baseline demand for Unproven DSR CMUs with Capacity Agreements for capacity obligations which begin to have effect in the 2020/21 Delivery Year, and allow the use of historic data for DSR CMUs with Capacity Agreements for capacity obligations which begin to have effect in the current Delivery Year (2019/20) in relation to its SPD tests.

C.3.2.1 Summary of responses

A majority of respondents either supported or did not comment on the DSR baseline demand easement. A small number of respondents expressed concern that the proposal could lead to inaccuracy, gaming, and overstating of DSR volumes, although they recognised the need for a relaxation of the Rules due to the challenges presented by the effects of the coronavirus. Two respondents suggested this easement does not maintain a level playing field, with one stating similar easements should be extended to New Build CMUs and Refurbishing CMUs and another stating use of historical data should apply to all CMUs or none.

One respondent welcomed the proposal but expressed concern that they were not far reaching enough as it would not help those sites that are already shutdown. It was also suggested that we should allow DSR providers to test Unproven DSR CMUs during the pre-qualification period.

C.3.2.2 Government response

The Government recognises that a shorter baseline period potentially increases the potential for an inaccurate baseline to be established. That said, we are also aware of the difficulties that DSR providers may face in establishing a baseline over an extended period due to the effects of coronavirus. Our objective is to help DSR providers achieve timely delivery, and so be in a position to contribute to security of supply this winter. We believe that reducing the period over which to establish a baseline will help achieve this objective. That said, in response to concerns from respondents, the baseline period will be reduced to three working days, rather than two as originally proposed in the consultation, from the six week period preceding the day on which the DSR Test occurred.

C.4 Appeals easements

C.4.1 Modifications to Secretary of State's appeals discretion

Consultation proposal:

Allow longer period for a person to appeal to the Secretary of State, the Delivery Body and the Authority, if the person meets certain criteria.

Increase the time the Secretary of State can grant as an extension before an agreement is terminated to enable compliance with a specified requirement.

Introduce new termination event that carries no termination fee where non-compliance arises from the coronavirus pandemic or related restrictions.

C.4.1.1 Summary of responses

16 respondents submitted comments on the proposed modification to the appeals process.

C.4.1.1.1 General approach

The respondents welcomed the proposed easement of the appeals process and were generally in favour of the proposed extensions to appeals timeframes. They felt the changes were proportionate and would allow parties to take comfort that they would have some additional leeway to appeal adverse decisions, which would help rebuild investor confidence, thereby enabling successful delivery, reducing terminations and preserving capacity to contribute to security of supply.

Several respondents noted that where the Secretary of State's discretion is applied, either in determining the termination fee or allowing an extension period, visibility and transparency of the process would be important.

One stakeholder suggested that the wording of the Regulations describing the Secretary of State's discretion should not be overly prescriptive, to allow the Secretary of State flexibility to consider any issues arising from the coronavirus pandemic that have not been addressed within this consultation.

A small number of respondents noted that the termination of a Capacity Agreement can have broader impacts on the Capacity Provider. The examples given related to: Rule 5.4, where the provisions for a Defaulting CMU can restrict the CMU's ability to participate in subsequent auctions; and Rule 6.8.2D, where the termination of a Capacity Agreement for a New Build Interconnector CMU also terminates any subsequent Capacity Agreements for that CMU. As such, where a Capacity Provider's circumstances can be shown to be a result of the effects of coronavirus, the respondent advocated allowing the Secretary of State to apply discretion in relation to these rules.

Finally, a number of respondents suggested that Regulation 69(5) be modified so that corrections or any additional documents / supporting evidence which should have been

provided during Prequalification can be submitted so that applications are not rejected if errors arise due to operational restrictions during lockdown.

C.4.1.1.2 Increasing the time the Secretary of State can grant as an extension

Several respondents highlighted that, given the proposed additional flexibility for the Secretary of State to grant a longer extension would only be available in the first Delivery Year of an agreement, which coincides with the Long-stop Date for prospective CMUs, those CMUs that miss their Long-stop Date would not be able to seek a further extension of 12 months through the appeals process.

C.4.1.1.3 New termination event

Several respondents raised concerns about the introduction of a termination event without a relevant termination fee attached. They felt this could limit the incentive for CMUs to deliver as soon as practicable during a Delivery Year. It was recommended that incentives to deliver should be considered by the Government prior to the laying of Regulations.

It was recommended that any proposal for a termination event without a fee attached to it should be backed up by clear criteria to identify under what circumstances this might apply. It was suggested that the Government publish guidance detailing how appeals from Capacity Providers requesting the application of this termination event would be assessed, what criteria would be used and what evidence would be required.

Clarification was requested by several stakeholders as to why the application of the new termination event was proposed to be limited to the first Delivery Year of a Capacity Agreement.

C.4.1.2 Government response

C.4.1.2.1 General approach

In line with the majority view of respondents, the Government intends to proceed with the modifications to the appeals process as proposed in the consultation. Specifically we will: allow a longer period for a person to appeal to the Secretary of State, the Delivery Body and the Authority; increase the time the Secretary of State can grant as an extension before an agreement is terminated; and introduce a new termination event that carries no termination fee where non-compliance is owing to the exceptional circumstances of the Capacity Provider's situation arising from the effects of coronavirus. We are not minded to introduce a self-termination event, capacity providers will still only receive termination notices for failing to meet milestones, or becoming insolvent, as we feel this is proportionate to the impact of coronavirus.

These modifications will apply to agreements awarded in auctions that took place before 1 April 2020, rather than those that existed on 1 April 2020, as proposed in the consultation. This is to clarify the intention that the modifications should apply to agreements awarded in the recent T-3, T-4 and T-1 auctions which had a 'coming into force' date of 1 May 2020.

We acknowledge the desire for greater transparency of the decisions to grant extensions or waive termination fees. In this regard, we note that the outcome of each appeal will be recorded on the CM register. However, we do not intend to publish the details of the reasoning

for the decisions made in respect of individual appeals as this information is often of a sensitive nature and commercially confidential.

The Government does, however, intend to update the appeals guidance for applicants[44] providing information on the criteria against which appeals seeking to rely on either the extended timeframe or new termination ground will be assessed, and the type of evidence required.

The Government notes that terminations can sometimes have broader impacts beyond the imposition of termination fees and the repayment of Capacity Payments. However, we do not intend to make any changes to these arrangements given that, if a Capacity Provider successfully appeals a termination notice on the merits of the specific case, then the termination notice is withdrawn and the 'broader impacts' do not materialise.

The Government does not intend to relax Regulation 69(5) of the Regulations to allow the Delivery Body to take into account new information provided as part of a request for reconsideration of a reviewable decision. Experience from the last two rounds of Prequalification has demonstrated that the vast majority of applicants are able to successfully meet the current requirements. We believe that a modification to Regulation 69(5) is likely to lead to uncertainty and may cause delays and so act counter to our objective in making these easements. Further improvements to Prequalification, as part of business as usual development, are planned for this year and should continue to aid applicants in prequalifying their CMUs.

C.4.1.2.2 Increasing the time a Capacity Provider can appeal a termination and the time the Secretary of State can grant as an extension

In respect of agreements awarded in auctions held before 1 April 2020 in respect of which the Delivery Body has given a termination notice before 1 May 2021, the Government intends to modify Regulation 33 to allow Capacity Providers an additional ten working days to bring an appeal to the Secretary of State (from 20 to 30 working days following the date a termination notice is given). We feel this is proportional to the disruption caused to Capacity Providers who wish to access the appeals process by the effects of coronavirus.

In respect of agreements awarded in auctions held before 1 April 2020, we also intend to modify Regulation 33 to allow Capacity Providers to ask the Secretary of State to consider granting termination notice extensions of up to 12 months instead of the current six months if the request is made in the delivery year of a single year agreement or during the first delivery year for a multi-year agreement. The Government also intends to allow the Secretary of State the discretion to extend terminations by up to 12 months.

We note that these changes will cover most agreements. The small number of Capacity Providers with multi-year agreements awarded in the T-4 auction for Delivery Year 2019/20 who have not yet delivered, and intend to make use of the extended long-stop date provisions, would only be able to take advantage of this additional time for termination notices issued before 1 October 2020. This is because, after that date they would no longer be in their first delivery year. We feel that this is equitable and proportionate given the changes we have made to provide an extended long-stop date for this group.

[44] https://www.gov.uk/government/publications/capacity-market-appeals-process

C.4.1.2.3 New termination event

With respect to concerns that termination on the new ground for which no termination fee is payable may undermine delivery incentives, the Government notes that each appeal will be considered on its own merits and a decision made in relation to the facts in each case. Given there is no guarantee that the Secretary of State will decide to exercise the discretion to terminate on that ground, Capacity Providers should remain incentivised to deliver.

The rationale for limiting the application of the new termination event to appeals made by Capacity Providers by the end of first Delivery Year of a multi-year agreement is that it would not be proportionate to allow the modifications to the Secretary of State's discretion to apply beyond that time. For example, year 15 of an agreement secured in the T-4 auction held in 2020 would be 2038. Given the short timeframe that was possible for the consultation, it is important that the modifications are temporary and only in place as long as strictly necessary to support CM participants in dealing with the effects of coronavirus. The Government will keep under review whether additional modifications are necessary over time.

C.4.2 Amendments to appeals of Delivery Body reviewable decisions and appeals to the Authority

C.4.2.1 Summary of responses

Consultation proposal:

Allow a longer period for a person to appeal to the Secretary of State, the Delivery Body and the Authority, if the person meets certain criteria.

Allow the Delivery Body longer to consider a request to reconsider a "delivery body reviewable decision" (including the issue of termination notices and Prequalification decisions).

Most respondents did not comment on this aspect of the proposal. One respondent requested clarification as to why the Delivery Body needed more time to reconsider a "delivery body reviewable decision" for decisions notified before 1 May 2021. They noted that there are very few decisions that are reviewable and to allow them more time, when the process is already slow, is not helpful to persons appealing.

C.4.2.2 Government response

In respect of delivery body reviewable decision notified before 1 May 2021, the Government intends to modify Regulation 69 to allow a person ten working days from the date on which they receive notice of a delivery body reviewable decision to request that the Delivery Body reconsider a delivery body reviewable decision. This gives an additional five working days, which is a proportionate response to the impacts on participants' access to this review process arising from the effects of coronavirus.

We also intend to modify Regulation 69 to provide the Delivery Body with 25 working days after giving notice of such decisions to reconsider such decisions if requested to do so. This nominally gives an additional ten working days but, in practice, only gives an additional five

C.5 Other issues raised

C.5.1 Summary of responses

18 responses were received which contained feedback that was either beyond the scope of the Easements Consultation or did not closely align with the proposals. These responses have been grouped into six themes and are summarised below.

C.5.1.1 Prequalification

There were several requests for the Government and the Delivery Body to support Capacity Providers in making Prequalification as practical as possible.

Several respondents requested early guidance on the timings of Prequalification in 2020 to support their planning and preparation.

A request for the use of electronic signatures from company directors was made by a number of respondents who noted this would be beneficial if working from home practices are still in place during Prequalification.

A few stakeholders requested an extension to the date by which Planning Consents need to be submitted, where consent is delayed as a result of the effects of coronavirus, and/or the temporary removal of the requirement for documentary evidence showing that the end date of the Relevant Planning Consent is after the expiry date of the Capacity Agreement.

C.5.1.2 Transparency

Some respondents requested that the Delivery Body publish information outlining the extent to which the proposed easements had been used and identifying any impacts on security of supply. Respondents felt this would promote market transparency. One respondent noted the number and capacity of CMUs accessing easements, in consideration of commercial sensitivities, should be made available in an aggregated format, including total aggregated volume of CMUs that would be unavailable to deliver. Respondents felt this information would enable them to develop their own analysis to the risk of a stress event and how to fill capacity gaps.

Several respondents requested the Government share a consolidated version of the Rules ahead of Prequalification to support Capacity Provider's understanding of the Rules changes.

C.5.1.3 Additional Rules change suggestions

Three respondents felt that changes to Rule 4.4.4 would be appropriate in supporting Capacity Providers by enabling changes the configuration of their CMUs, provided their capacity obligation can still be met.

C.5.1.4 Expansion of easements

Several respondents highlighted that the effects of the coronavirus pandemic may have long-term impacts and affect CMUs not supported by the proposed changes in the Easements Consultation (e.g. CMUs with agreements for Delivery Years beyond 2020/21). A number of

respondents felt the Government should continue to monitor the need for additional flexibilities and easements depending on the continuing effects of the coronavirus.

A couple of respondents requested a Force Majeure clause be added to the Rules. One respondent also suggested the proposed legislation be expanded to allow the Secretary of State direction to expand easements as required.

C.5.1.5 Secondary trading

One respondent requested guidance on how the secondary trading market could be made more flexible to mitigate the potential risks resulting from the coronavirus pandemic.

C.5.1.6 The Financial Commitment Milestone

Three respondents noted that the deadline for the Financial Commitment Milestone for agreements awarded in the 2020 T-3 Auction occurs in the Autumn. They suggested that the deadline should be extended to match the typical deadlines for a T-4 auction.

C.5.2 Government decision

C.5.2.1 Prequalification

The Government recognises the need for clarity on Prequalification in 2020 and we will work with CM Delivery Partners to publish guidance as soon as reasonably practicable.

We note respondents' requests for electronic signatures during Prequalification. Scanned electronic signatures on Exhibits and similar PDF documents will be acceptable in Prequalification, but applicants should ensure scanned signatures are used only by those with the authority to make the authorisation.

The deadlines associated with planning consents do not arise until 2021, therefore we do not intend to make any changes for now but will keep the need for any further extensions or easements under review.

C.5.2.2 Transparency

The Government notes the request for the Delivery Body to publish information outlining the extent to which proposed easements have been used. The Government and its CM Delivery Partners will work closely to monitor the effects of coronavirus on security of supply.

The amending Rules and Regulations to implement the proposals outlined in this response will be published in the usual way. A consolidated version of the Rules showing the temporary modifications will be published shortly after the Rules are laid in Parliament.

C.5.2.3 Additional Rules change suggestions

We note the request for changes to Rule 4.4.4. However, such amendments were not consulted on in the Easements Consultation and it would not be appropriate to make enduring changes to the Rules following such a limited consultation. We note that Ofgem have

Annex 2 – Assessment of Impacts

Annex 2.1 Assessment of Impacts for the Future Improvements Consultation

Annex 2.1.1 Allowing Unproven DSR to access multi-year agreements

Overall, we expect the impact of allowing Unproven DSR to access multi-year agreements to be small, albeit there may be some minor beneficial impacts from increased auction liquidity. We expect very little DSR will be able to meet the CAPEX thresholds required for multi-year agreements. The overwhelming majority of respondents to the consultation agreed with this assessment, noting that DSR projects are not typically capital intensive. Whilst some forms of DSR (e.g. new build behind-the-meter-generation) may be more likely to have high capital expenditure, these projects are already able to qualify as New Build CMUs in order to access multi-year contracts and so there might not be much additional demand for multi-year contracts from these types of DSR.

As pointed out by respondents to the consultation, some positive impacts may arise because multi-year agreements could reduce the administrative burden of annual Prequalification requirements, thus encouraging greater participation in the CM auction by DSR. That said, we do not expect this will have a significant impact given the small number of DSR CMUs that may be able to meet the CAPEX thresholds. Some DSR CMUs which meet the CAPEX thresholds may also not wish to be tied into long term agreements (especially up to 15 years) and so not participate on that basis.

If the number of DSR CMUs entering the auction were to increase as a result of allowing DSR to access multi-year agreements then, in addition to increased auction liquidity, there could also be increased costs on the Delivery Body and Settlement Body of administering the auction. However, given the very small number of DSR CMUs that may be able to meet the CAPEX thresholds, we expect the increase to the costs of running the auction to be negligible.

Annex 2.1.2 Reducing the Minimum Capacity Threshold to 1MW

Responses to the consultation suggested there could be increased participation in capacity auctions by units smaller than 2MW. However, smaller capacity is already able to participate in the auction by aggregating their capacity with other providers, so there might not be many more units that would now participate in the auction, other than those which are difficult to aggregate. Existing aggregated units may also decide to split into smaller components.

Available evidence suggests any increase in auction liquidity due to participation by units smaller than 2MW is likely to be negligible. The second transitional CM auction (Delivery Year 2017/18) had a minimum threshold of 0.5MW, but only 2 units smaller than 2MW participated out of a total of 47. In the T-4 and T-1 auctions run to-date, participating units sized between 2-3MW make up much less than 1% of the total capacity participating in the CM and around 5% of units participating in auctions to-date. Due to the small size of such units it would take a very substantial increase in unit numbers to have a noticeable impact on auction volumes and liquidity.

An increase in the number of units participating in the auction could increase costs on the Delivery Body and Settlement Body of administering Prequalification, registration, metering assurance etc. as was noted by one respondent to the consultation. This impact will depend on the number of additional units as well as factors such as how many components they contain (if they are DSR). Overall, whilst it is uncertain how many additional units may participate due to lowering the threshold, the total impact is likely to be small, based on feedback received from the consultation and experiences from previous auctions.

Annex 2.1.3 Amending the T-1 set-aside commitment and methodology

We do not anticipate that this change will have an impact on the CM or on security of supply as the set-aside has been determined using this methodology since 2016, and the amendments to the Regulations merely formalise the process.

Annex 2.1.4 Incorporating new technologies

We do not anticipate that this change will have an impact on the CM or on security of supply as the Government regularly reviews whether new capacity types have emerged, and this merely formalises the process.

Annex 2.1.5 Emission limits

The impacts of introducing emission limits in the CM are considered in Annex 2.2.

Annex 2.1.6 Long-term STOR

Removing the exclusion on LT STOR may slightly increase the capacity eligible to participate in the CM auctions, by up to about 0.4GW, based on National Grid ESO's STOR market information report.[48] However, some LT STOR units may choose not to participate in the CM and/or LT STOR contract holders may not be able to meet the new emission limits in order to participate in the CM from 2024. This may reduce the amount of LT STOR capacity that can participate in the CM auctions, once the exclusion is removed.

Whatever additional participation there is from LT STOR units, the auction target will be increased by the same amount[49], because the capacity of LT STOR contracts is currently deducted from the CM auction targets. Therefore, there will be no overall impact on liquidity. The slightly higher target could increase the cost of the CM, but we cannot quantify this additional cost as it depends on the amount of LT STOR that participates as well as clearing prices for future auctions, which are uncertain.

For illustration, we consider the highest and lowest clearing prices seen in the T-1 and T-4 auctions to date, £0.77/kW/year in the T-1 for delivery in 2019/20 and £22.50/kW/year in the T-4 for delivery in 2020/21. If all LT STOR contract holders participated in the CM, using those illustrative prices, removing the exclusion could increase costs by around £0.3m - £9m per year. For context, the total cost of the CM is around £1bn per year. As such, we expect the

[48] www.nationalgrideso.com/document/154431/download

[49] When recommending the target to procure at auction, National Grid ESO estimate the capacity required to meet the reliability standard (established in 2014 to indicate an acceptable level of security of supply). They then deduct capacity not participating in the auction (for example low carbon plant receiving Contracts for Difference payments), these deductions previously included capacity with a LT STOR agreement. If LT STOR capacity choose to participate in the auction in future, their capacity will no longer be deducted from the auction target and the target will be higher.

cost of removing the LT STOR exclusion to be less than 1% of the total annual cost of the CM, so overall the impact is relatively small.

Annex 2.2 Assessment of Impacts for the Emission limits Consultation

Emission limits taking effect on 1 October 2024 rather than 1 July 2025 will prevent plants that emit more than 550g of CO_2 per kWh and more than 350 kg CO_2 on average per year per installed kW participating in the CM in Delivery Year 2024/25. Figures on emissions by technology drawn together for a Parliamentary Question[50] show that estimated CO_2 emissions are higher than 550g/kWh for coal and diesel reciprocating engines (790g/kWh and 602g/kWh respectively). Gas reciprocating engines and open cycle gas turbines (OCGTs) have estimated typical emissions of 497g/kWh and 460g/kWh respectively, so it's possible that low efficiency plant using these technologies could also be affected. However, even if they are above this threshold, to be affected by the measure their running hours would also need to be high enough that they emit more than 350kg CO2 per kW per year.

It is uncertain how much high emission plant would have participated in the auction for Delivery Year 2024/25. However, to give an indication of scale we can look at the results of the auction for Delivery Year 2023/24. About 1.3GW of coal capacity was successful and may have also won agreements in 2024/25. However, the Prime Minister announced in February 2020 that, subject to consultation, the Government will bring forward the date for closing unabated coal from 1 October 2025 to 1 October 2024. If this policy is implemented, imposing emission limits in the CM from 1 October 2024 would have no effect on coal operators as they would be required to close anyway. According to published CM registers, the only units with a primary fuel type of diesel or distillate to win agreements for Delivery Year 2023/24 were OCGTs. Combined with gas fuelled existing OCGTs and gas fuelled reciprocating engines, over 2GW of capacity potentially affected by emission limits won agreements for that year. It is unclear how much of this capacity could be affected by the limits, but we expect it to be small as typical emissions for these technologies do not breach the emission limits and they were barely mentioned by respondents to the consultation.

Preventing these plants from participating in the CM could increase the costs of the auction as the capacity could be replaced by more expensive plant. It could also lead to the closure of affected plant entirely, leading to changes in the generation mix, emissions and the cost of the electricity system. However, if coal closure is brought forward to 1 October 2024, we expect the amount of capacity affected to be very small and, therefore, for the impact on the electricity system to be very small.

Even if the date for phasing out unabated coal is not brought forward, the coal load factor is likely to be very low (it was around 6% in 2019[51]) and the timescale considered (one year) is short so we expect the impact of this change to be small. The small magnitude of the impact, coupled with uncertainty over key parameters (including gas, coal and carbon prices), makes precise estimate of any impacts difficult. Further detail on the impact of coal closure by 2025

[50] https://www.parliament.uk/business/publications/written-questions-answers-statements/written-question/Commons/2015-11-26/17799/
[51] Source: Aurora Energy data

can be found in the 2018 Impact Assessment[52] and updated analysis is planned to be published in due course.

Annex 2.3 Assessment of Impacts for the Coronavirus Consultation

These measures have the effect of, temporarily, removing or relaxing obligations and deadlines to reduce administrative and operational burdens and minimise the likelihood of terminations which arise from the effects of coronavirus or the restrictions imposed by the Government to tackle it, that are outside of capacity providers control.

The impact of these measures is likely to be small due to the small amount of capacity that could be affected. That said, the flexibility in these deadlines and obligations should lead to fewer terminations and fewer capacity providers having to halt operations which could usefully deliver capacity at a later point over the winter. Therefore, we expect the measures to slightly reduce risks to security of supply in the medium to long-term and maintain levels of CM payments

Whilst the measures relax obligations and deadlines in the short-term, we do not expect this to have an adverse effect on short-term security of supply, because projects whose delivery time frames are delayed due to the effects of coronavirus would not have met their obligations and deadlines anyway. The measures simply ensure that these projects are allowed additional time to reach completion, without having their capacity agreement terminated. Whilst these measures may slightly weaken the incentives to complete projects promptly, by postponing the threat of termination fees, there is still a financial incentive for capacity providers to deliver as soon as possible because capacity payments will not be made until projects are complete.

In 2019, similar modifications to some CM obligations and deadlines were made in response to the standstill period. This resulted in very low amounts of capacity being terminated. Only around 250MW (4%) of T-1 agreements for Delivery Year 2018/19 and 30MW (1%) of T-1 agreements for Delivery Year 2019/20 were terminated (as of May 2020). All T-4 terminations for those Delivery Years occurred before the standstill period began.

Therefore, on balance we expect the net impact on security of supply to be positive. The amount of capacity affected by these measures is difficult to quantify as we have limited information on how many units have been substantially affected by the coronavirus, however the sections below provide a possible indication of scale.

Annex 2.3.1 Satisfactory Performance Days

This measure removes the effect of the suspension of capacity payments if a CMU fails to demonstrate three separate SPDs during the 2019/20 winter.

The Delivery Body's data shows that the vast majority of capacity for Delivery Year 2019/20 has completed its SPDs and there is very little capacity whose SPDs are outstanding, so we expect the maximum capacity that could be affected by the measure to be very small.

[52] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/672137/Government_Response_to_unabated_coal_consultation_and_statement_of_policy.pdf

Annex 2.3.2 Metering Tests

This measure extends the metering test deadline from 17 September to 30 September 2020 for Existing CMUs, Pre-Refurbishing CMUs, Proven DSR CMUs and Unproven DSR CMUs holding T-1 agreements for capacity obligations for Delivery Year 2020/21.The impact of this measure is expected to be negligible as, out of the 55,000MW of capacity with agreements for 2020/21, only around 10MW of this capacity won an agreement in T-1 and requires a metering test.

Annex 2.3.3 Long-stop Date extension

This measure extends the Long-stop Date by 12 months for New Build CMUs awarded T-1 agreements which start in Delivery Year 2020/21, Refurbishing CMUs with multi-year agreements which start in Delivery Year 2020/21 and New Build CMUs awarded T-4 agreements which were due to start in Delivery Year 2019/20 (i.e. have a Long-stop Date of 30 September 2020).

Data from the Delivery Body shows that there is only a small amount of capacity with a Long-stop Date of the start of the Delivery Year 2020/21 that has not already completed their SCM or MCR, therefore the overall impact of this measure is expected to be low. This is the maximum capacity that could be affected by this measure. We do not know how much of it may be delayed.

Annex 2.3.4 Independent Technical Expert reports

This measure removes the requirement for an ITE report in relation to Six Monthly Progress Reports and any associated remedial plan, falling due during the 2020/21 financial year for New Build CMUs and Refurbishing CMUs. It also removes the requirement for a remedial plan to be submitted by CMUs that are eligible for the Long-stop Date extension.

We are unable to quantify this impact as we do not know how many CMUs would have been required to provide an ITE report or remedial plan, were the measure not in place.

Annex 2.3.5 Unproven DSR Metering Assessment, Metering Test and DSR Test Deadlines

This measure gives DSR aggregators with Unproven DSR CMUs holding T-1 or T-4 agreements for capacity obligations which begin to have effect in the 2020/21 Delivery Year an additional 12 months to comply with the Metering Assessment, Metering Test and DSR Test deadlines.

We are unable to quantify this impact as we do not know how many CMUs would have missed the original deadlines. To give an indication of the potential scale, there is about 1.4GW of Unproven DSR holding T-1 or T-4 agreements beginning in the 2020/21 Delivery Year. This is the maximum capacity that could be affected.

Annex 2.3.6 DSR baseline demand

This measure shortens the period for establishing a baseline of demand for DSR CMUs to three working days (rather than two as originally proposed in the consultation) from the six week period preceding the day on which the DSR Test occurred.

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