



Department for
Business, Energy
& Industrial Strategy

Capacity Market

Rules Amendments to Improve Auction
Liquidity

Closing date: 22 June 2022



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Executive summary

This consultation seeks views on two time-limited proposals designed to improve liquidity in future Capacity Market (CM) auctions. We have developed these proposed changes to the Capacity Market Rules (CM Rules) which, if not delivered as a matter of urgency, could unnecessarily restrict participation in the 2023 capacity auctions.

Whilst the NGESO have not yet completed their analysis for the winters ahead, we expect that the target for the 2023 T-1 capacity auction (for delivery year 2023/24) is likely to be stretching.¹ Therefore, it is prudent to take steps ahead of prequalification to ensure that the participation in the auction is maximised. We have identified some potential barriers to entry, that are set out in this consultation, which we would propose to remove for the 2022 Prequalification Window.

We believe these proposed measures are necessary to facilitate the CM in achieving its objective of ensuring security of electricity supply in Great Britain in future years at least cost to consumers.

The proposals are as follows:

- **Postponement of the introduction of the statutory requirement for independent verification of fossil fuel emissions:** Given delays to the accreditation process there is no guarantee that there will be sufficient availability of accredited Independent Emission Verifiers (IEVs) for this year's Prequalification Window. This proposed measure, which effectively rolls over arrangements from previous years, is necessary to mitigate the risk of Applicants failing to prequalify for the 2023 CM auctions as a result of potential inability to access emissions verification services.
- **Amendments to arrangements on mothballed plant:** This proposed measure is necessary to remove a barrier to prequalification for mothballed plants that would otherwise prevent their prequalification for the 2023 CM auctions.

This consultation will run for **two weeks** until 22 June 2022. We will then consider responses received in determining whether to implement proposals. The short consultation period is necessary to ensure that, should we decide to implement our proposed changes, we have time to do so before the Prequalification Window for the next auction round opens in July 2022.

¹ A change made last year to how NGESO model non-delivery led to a higher T-1 target and it is likely that this methodological change will have a similar impact on the next T-1 target.

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1. General information

1.1 How to respond

This consultation will run for **two weeks** until 22 June 2022. We will then consider responses received in determining whether to implement our proposals. The short consultation period is necessary to ensure that, should we decided to implement our proposed changes, we have time to do so before the Prequalification Window for the 2023 auction round opens in July 2022.

Email to: electricity.security@beis.gov.uk

When responding, please state whether you are responding as an individual or representing the views of an organisation.

Your response will be most useful if it is framed in direct response to the questions posed, though further comments and evidence are also welcome.

1.2 Confidentiality and data protection

Information you provide in response to this consultation, including personal information, may be disclosed in accordance with UK legislation (the Freedom of Information Act 2000, the Data Protection Act 2018 and the Environmental Information Regulations 2004).

If you want the information that you provide to be treated as confidential please tell us, but be aware that we cannot guarantee confidentiality in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not be regarded by us as a confidentiality request.

We will process your personal data in accordance with all applicable data protection laws. See our [privacy policy](#).

We will summarise all responses and publish this summary on [GOV.UK](#). The summary will include a list of names or organisations that responded, but not people's personal names, addresses or other contact details.

1.3 Quality assurance

This consultation has been carried out in accordance with the government's [consultation principles](#).

If you have any complaints about the way this consultation has been conducted, please email: beis.bru@beis.gov.uk.

2. The proposals

2.1 Verification of Fossil Fuel Emissions Declarations

Context

Under the CM's Emissions Limits framework, all Applicants with Fossil Fuel Components are required to provide a Fossil Fuel Emissions Declaration that demonstrates compliance as part of their application. Since the introduction of Emissions Limits to the CM in 2019, it has been our policy intent to introduce independent verification of Applicants' declared emissions. However, the introduction of the requirement for independent verification of emissions declarations has previously been postponed due to the timeframes needed for the accreditation of Independent Emissions Verifiers (IEVs) for the CM. As things stand, IEV checks will be required for all Fossil Fuel Emissions Declarations from the 2022 Prequalification Window onwards, in line with Rule 3.15.1.

The United Kingdom Accreditation Service (UKAS) is the organisation responsible for the accreditation of IEVs in the UK.² Accreditation is currently underway, and information on the current status of the process is published on UKAS' website.³ Although UKAS aims to complete several accreditations in advance of the 2022 Prequalification Window, a number of factors have caused significant delays to this work, and there is no guarantee that sufficient numbers of IEVs will be available for the 2022 Prequalification Window.

This creates the risk of bottlenecks forming if multiple Applicants were to seek to access the services of too few IEVs (or, in an extreme scenario, if no IEVs are available at all). This, in turn, risks creating a barrier to entry into the CM, in that some Applicants could fail to secure the required verification services and fail to prequalify as a consequence. In a worst-case scenario, significant numbers of Applicants could be impacted by such constraints on IEV capacity.

Proposal

We therefore propose to delay the introduction of the statutory requirement for Fossil Fuel Emissions Declarations to be verified by an IEV until the 2023 Prequalification Window. We intend to deliver this postponement in a way that does not impact on any other obligations arising under the CM Rules. A postponement of the requirement for IEV checks was delivered in 2021; we are therefore confident that a similar action could be taken without disruption to the CM's broader functioning.

² The CM Rules allow for persons established outside of the UK to be accredited as IEVs by the relevant authorities as set out in Rule 1.2.1. However, the government is not currently aware of any persons meeting these requirements.

³ This is available at <https://www.ukas.com/accreditation/about/developing-new-programmes/development-programmes/ecm-verification/>

Impact

We would expect that any implementation of the proposed temporary measure would facilitate a continuation of the current functioning of the CM for the 2023 auctions.⁴ Failure to implement this measure would potentially have considerable impacts. Constraints to IEV availability would create a barrier to entry for Applicants and could result in otherwise eligible capacity failing to prequalify due to an inability to procure the necessary IEV certification. This would reduce competition in the 2023 auctions, causing an increase in the clearing price and higher costs being passed on to electricity consumers. There is also a possibility that the volume of capacity able to prequalify and participate in the 2023 auctions would be lower than the auction target itself, so the auctions would procure below the auction target. As the auction target is informed by the Reliability Standard, this may lead to risks to security of supply.

There is uncertainty over how long UKAS' accreditation process will take, so it is not possible to provide a more detailed assessment as to the extent of potential IEV capacity constraints, nor of the risk that Applicants could fail to prequalify as a result. However, given the potential risks to auction liquidity outlined above, we consider this proposal would be a reasonable precaution to take.

We acknowledge that delaying the requirement for validation by IEVs could theoretically lead to a risk of higher carbon emissions from falsified claims. However, we consider this risk is low as the proposed measure only seeks to implement a temporary relaxation of the requirement. To date, BEIS has received no evidence that there has been any falsification of Fossil Fuel Emissions Declarations previously.

Question 1

What are your views on the proposal to postpone the introduction of the statutory requirement for Fossil Fuel Emissions Declarations to be independently verified until the 2023 Prequalification Window?

2.2 Mothballed capacity

Context

It has been brought to our attention that the CM Rules (specifically Rule 3.6.1a) may prevent existing generating CMUs, which have been mothballed for more than 24 months prior to the end of the Prequalification Window, from prequalifying for the 2023 auctions. Rule 3.6.1a covers previous operational performance data. It requires Applicants for existing generating CMUs to identify three Settlement Periods on separate days in the 24 months prior to the Prequalification Window in which the CMU delivered a net output equal to or greater than its Anticipated De-

⁴ I.e. the T-1 auction for the 2023/24 Delivery Year and the T-4 auction for the 2026/27 Delivery Year.

Rated Capacity and to report the operational data for each of those Settlement Periods. The purpose of Rule 3.6.1 is to demonstrate that the existing generating capacity is real and capable of generating.

In 2018, Ofgem made amendments to Rule 3.6.1a⁵, following a statutory consultation held on the CM Rules. Prior to this change, Rule 3.6.1a allowed existing generating CMUs that had not been operational for 24 months prior to one month before the Prequalification Window to use operational data that was more than 24 months old to demonstrate performance under this criterion.

Rule 3.6.1a was amended by Ofgem in 2018 to ensure that the historical data being provided by Applicants was representative of performance, and to simplify the CM Rules in this area as 3.6.1a had been the subject of several prequalification disputes due to a lack of clarity. Ofgem decided to amend Rule 3.6.1a so that all three settlement periods fell within a 24-month window ending on the day that the Prequalification Window opens. They also adjusted the wording of the CM Rules to improve clarity. Their rationale for shortening the window for data was as follows:

'To ensure that the periods specified by the generator are recent enough to be representative of the generator's performance, but allow enough time for generators to prove their capacity if – for example – they are mothballed or unavailable.'

One respondent to Ofgem's consultation in 2018 commented that the change would exclude plants mothballed for more than 24 months. Ofgem's response to this was as follows⁶:

One stakeholder suggested that there may be circumstances in which an Applicant has capacity which has not been demonstrated in the specified 24-month period (for example, because a unit was mothballed). We believe that such scenarios are likely to be rare. We continue to believe that historical output in a 24-month period provides a good balance between accurately reflecting an Applicant's capacity, and not excluding capacity that has been mothballed for a short period.

We are now aware of plants of a significant size which cannot meet Rule 3.6.1a. The 2023 T-1 auction may be at risk of not procuring sufficient capacity to meet the auction target. We accordingly wish to ensure that plants of this kind are not precluded from prequalification for the 2023 auctions by this Rule. This will help ensure the best chance of procuring sufficient capacity and continuing to meet our Reliability Standard for winter 2023/24.

Stakeholders have indicated that it may be possible for existing plants that have been mothballed for more than 24 months to prequalify under the existing CM Rules, if they enter as a Refurbishing CMU which then reverts to a Pre-Refurbishment CMU if the refurbishment works are not completed on time. We are not supportive of any proposal that would cause Applicants to knowingly fail to meet CM milestones and consider it does not align with our policy intent. Therefore, we believe that there remains a strong rationale for the proposals below.

⁵ <https://www.ofgem.gov.uk/publications/publication-consolidated-capacity-market-rules-2018>

⁶ <https://www.ofgem.gov.uk/publications/publication-consolidated-capacity-market-rules-2018>

Proposal

We propose to make amendments which allow – once more – existing generating CMUs to demonstrate performance using operational data from the most recent 24 months of operation if there is no data from the 24 months of operation prior to the closure of the Prequalification Window.

Given the urgency behind this proposal, we propose that if this measure were to be implemented, it would be done through via a time-limited modification to the CM Rules, which will mean that the change will only apply for the 2022 Prequalification Window. We will then review the CM Rules relating to operational performance data again in due course, to assess whether it is working as intended and whether any enduring changes may be required.

We are not at this stage intending to make any enduring changes, because we have concerns that doing so at speed could create opportunities for speculative bidding by mothballed plants and/or diminish the accuracy of performance checks. As part of any enduring solution, we may consider proposing credit cover requirement for existing generating CMUs which do not have operational data for the 24 months prior to the close of the Prequalification Window and/or apply additional performance checks to such CMUs, in order to mitigate these risks. We consider that the risks outlined above do not outweigh the potential risk to energy security of not procuring sufficient capacity in the 2023 T-1 auction if relevant mothballed plants are not able to prequalify due to the identified issue above. Therefore, there is a strong rationale for a time-limited modification this year.

Impact

This measure would allow existing generating CMUs that have been mothballed for over 24 months to apply for prequalification for the 2023 auctions.⁷ We are aware of mothballed plants which may be affected by this measure.

If the target for the 2023/24 T-1 auction is similar to the previous T-1 auction in 2022, it is likely to be high relative to the volume of capacity able to participate in the auction. In a worst-case scenario, the volume of capacity able to prequalify and participate in the auctions would be lower than the auction target itself, so the auctions would procure below target. As the auction target is informed by the Reliability Standard, this may lead to risks to security of supply. Even if sufficient capacity can be procured, there may be a low level of liquidity in the auction. Making the amendments to the previous settlement period performance criteria as proposed would mean that existing generating CMUs that have been mothballed will not be precluded from prequalifying on this basis. This may allow additional capacity to participate in the 2023 auctions, enhancing the chances of procuring sufficient capacity in the auction and injecting additional competition into the auctions, which could lower the clearing price and improve our ability to meet the Reliability Standard for electricity security over winter 23/24.

The longer time period between the T-4 auction and the relevant Delivery Year allows new build plants to participate as there is sufficient time available for construction, so that auction is highly

⁷ I.e. the T-1 auction for the 2023/24 Delivery Year and the T-4 auction for the 2026/27 Delivery Year.

likely to secure the target capacity in the absence of this measure. However, if existing generating CMUs mothballed for more than 24 months are able to apply to prequalify for the 2023 auctions, it should also increase the level of competition and help put downward pressure on the auction clearing price and cost.

There is a risk that this rule change leads to capacity winning an agreement that it cannot deliver on due to, for example, problems whilst de-mothballing the generation capacity. However, there are other measures in place to incentivise delivery and test a unit's ability to deliver (such as Satisfactory Performance Days, penalties, and termination fees), so we view this as a low risk.

Overall, the measure is expected to increase participation and competition in the 2023 auctions. This will put downward pressure on the clearing price and, importantly for the 2023 T-1 auction, increase the likelihood of meeting the auction target. We are unable to quantify these impacts at present without knowing what the targets will be for the next set of auctions.

Question 2

What are your views on the proposed temporary changes to operational data requirements for existing generating CMUs? Does the proposed change create any unintended consequences? Are there any alternative ways to achieve the policy intent, beyond the changes discussed in this proposal?

3. Next steps

This consultation will run for **two weeks** until 22 June 2022. We will then consider responses and then publish our Government Response setting out our final determinations in due course.

This consultation is available from: <https://www.gov.uk/government/consultations/capacity-market-rules-amendments-to-improve-auction-liquidity>

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