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Submitted by email: EMR_CMRules@ofgem.gov.uk

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Dear Sirs,

Response from Enel X to the 5-year review of the Capacity Market Rules

Thank you for this opportunity to contribute to Ofgem's review of the Capacity Market Rules.

This response follows the structure of the consultation paper, although we have not responded to every question, and we have included comments on some other issues which should be in scope, but were not covered by the questions – e.g. the implementation details of Of12.

1 The objectives of the Rules

We view the capacity market as a permanent feature of the electricity system, and expect it to become more important over time as the system is further decarbonised.

We agree with Ofgem's view[1] that the Rules may have been appropriate for a market in which only a small number of large, centralised generators would participate, but they are not appropriate for a market with large-scale participation by distributed and demand-side resources. We welcome the intention to fix this.

Q1 Do you have any views on the interactions between the CM and other wholesale markets; such as forward markets, the balancing market, and markets for ancillary services?

To provide the desired level of security of supply at least cost, capacity market participation should be "stackable" with as many other value streams as possible. Otherwise, resources are forced to choose between participating in the capacity market and providing other services – reducing competition in the capacity market and increasing the costs borne by consumers. The concept of Relevant Balancing Services, in Schedule 4 of the Rules, goes some way towards fixing this, but only

[1] Consultation paper, ¶ 1.13.

for a short list of services that is unlikely to keep pace with reforms to balancing services.

As discussed at length in our response to your open letter,[2] we expect the lack of a dispatch mechanism for the capacity market to distort dispatch decisions. As well as unnecessarily increasing costs and restricting participation for DSR, this will also have a strong impact on wholesale markets and the balancing mechanism during and around the times of capacity market notices.

Q2 Do you have any evidence that design choices in the CM are driving inefficient outcomes in other markets?

There have not yet been enough Capacity Market Notices to provide evidence. However, as discussed in our previous submission, it is self-evident that the unique "design choice" to omit a dispatch mechanism will incentivise inefficient behaviour: resources self-dispatching when not needed, and erroneously not dispatching when actually they are needed. The first of these could easily lead to price reversals – i.e. prices falling around times of scarcity.

Q3 Do you have suggestions for how these markets can be better aligned and how any inefficiencies can be mitigated?

The lack of a dispatch mechanism should be remedied by introducing a dispatch mechanism, as discussed in our previous submission.

Relevant Balancing Services could be improved by replacing the narrow definitions in Schedule 4 of the Rules (in which a few specific services are supported, based on definitions found in various standard contract terms and other system operator publications) with a short list of principles. These should make it obvious which types of services are covered and what values are relevant, without being dependent on the services having particular names, or using particular sets of contract terms. Guidance publications – more easily updated than rules – can confirm how these principles apply to all balancing services of interest.

2 Ofgem's Rules change process

Q4 Do you have any views on whether the proposed membership of the CM Advisory Group is appropriate, the form of participation from industry, along with any further points regarding meeting frequency and function?

We consider it important that the group represent the breadth of technologies and organisations participating in the capacity market – not just the dominant ones.

[2] Enel X's response to the Government's Call for Evidence, 1 October 2018, which was also submitted to Ofgem in response to the open letter – especially pp. 8-12.

Q6 Do you have any feedback on our proposal to move to an 18-month implementation timescale; consulting on rule amendments which would subsequently be implemented the following Delivery Year?

We agree that the current annual cycle does not seem to be working well, as difficult changes, such as Of12, have been deferred repeatedly.

However, our impression is that the constraint is the level of resourcing available in the delivery partners. The headcount and budget for implementation and maintenance of capacity market systems seems to have been fixed before there was a good understanding of the scale of the work involved, apparently with no method for revisiting these decisions in the light of reality.

Since defects in the capacity market can have expensive impacts, fixing them should not automatically be deferred just because the work was not foreseen. Rather, the onus should be on the delivery partners to show that not only can they not do it with their current resources, but also the costs of additional resources would outweigh the national benefit from fixing the defect sooner.

Having said this, we do appreciate that system updates are easier with more notice. However, this new discipline would be for naught if other major changes were required without notice. We would therefore recommend that Government-initiated rule changes should be assessed through the same process.

Versioning of rules and regulations

There is often considerable confusion amongst participants as to exactly which versions of the rules and regulations apply. We recommend that, for both the rules and regulations:

- Consistent version numbering is used, with a new consolidated version issued each time any change is made.
- Whenever a new version is issued, it would be helpful also to publish a "delta" version highlighting the changes from the previous version.
- There should a table showing the dates between which each version of the rules and regulations is in force.
- Any "grandfathering" which deviates from these dates should be clearly explained.

We would draw your attention to the Australian Energy Market Commission's approach for managing the National Electricity Rules, which deals with version numbering very well. Since 2005, they have published 121 consecutively numbered versions of the rules. Each new version starts with a list of the changes

since the previous version, and notes any provisions which are not yet in force. A single table lists the dates that each version was in force.[3]

3 Regulatory burden – Prequalification

Q8 Do you believe the current length of the Prequalification window is appropriate and if allowing Prequalification submissions to take place throughout the year would be beneficial?

Allowing prequalification submissions throughout the year would be beneficial, so long as the Delivery Body assesses them promptly and provides feedback, allowing any errors to be rectified. This is the crucial change: moving from having only one shot at getting everything right to a more iterative process. This will reduce prequalification failures, and (more importantly, but less visibly) allow participants to put a reasonable amount of effort into prequalification, rather than inefficiently high levels, such as "three pairs of eyes on each submission".

Q10 Do you have any feedback on the amendments to the Prequalification data items listed in Table 1?

The changes set out in the table seem sensible. However, there is a related issue that we believe also needs attention: the deadlines for Metering Assessments and Metering Tests. Just as with prequalification, data should not be gathered unnecessarily early, as doing so precludes participation by some potential capacity providers.

For Existing Generating CMUs and Proven DSR CMUs that have been awarded a Capacity Agreement in a T-4 Auction, Rule 8.3.3(a)(i) requires them to complete a Metering Assessment 3 years ahead of the start of the Delivery Year.

This is an information-gathering exercise, just like prequalification, so it is something that should be done as late as possible. For sites that do not yet have metering that meets capacity market standards, this deadline forces the installation of new metering to be carried out 3 years earlier than necessary. It may then sit unused for 3 years. This seems wasteful.

The related Rule 8.3.3(e)(ii) requires such CMUs to provide a Metering Test Certificate 18 months ahead of the start of the Delivery Year. This is also wastefully early.

We note that, in its recent Consultation on Technical Amendments, the Government delayed the latter deadline for some Delivery Years:

[3] https://www.aemc.gov.au/regulation/energy-rules/national-electricity-rules/historical-versions

Given the metering test can be completed nearer to the start of the delivery year without affecting timely delivery, we intend to delay the deadline until 20 June 2020 or 5 months following the deferred capacity payment trigger event, whichever is the earlier.[4]

If the deadlines can be delayed without affecting timely delivery, then we recommend that they should be, for all Delivery Years. A sensible deadline for the Metering Test Certificate would be shortly before the final demand curve is set for the corresponding T-1 Auction. There is no obvious need for the Metering Assessment deadline to be much earlier.

5 Secondary trading arrangements

We are not convinced that the current version of Chapter 9 of the Rules is a good starting point for developing workable secondary trading arrangements, as it is too complex, with too many unnecessary details, leading to unintended consequences.

To give two examples of restrictions which seem to serve no useful purpose:

- A CMU with a Capacity Obligation of less than 2 MW is unable to trade its capacity away through secondary trading.[5]
- Although the Delivery Body's guidance[6] gives no hint of this, and their staff seemed unaware, CMU transfers are not possible for DSR CMUs, or for Generating CMUs where there is a change of Despatch Controller.[7]

These are just issues that we happen to have noticed recently. We are sure there must be many more such examples waiting to be discovered. We believe these errors were caused by the inappropriately restrictive style of drafting.

It would be better to start with a set of principles around secondary trading, and then strive to write the simplest and shortest set of rules that will implement those principles. The statement in ¶ 5.23 of the consultation paper would make a good principle:

Having the opportunity to trade the obligation to another party will enable capacity providers to make appropriate commercial decisions while maintaining the integrity of the CM and long-term security of supply, as well as value for money for consumers.

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4 BEIS, Technical amendments to the capacity market – Government response to consultation, p. 27.

5 Such CMUs exist, and are allowed, because Minimum Capacity Threshold in the General Eligibility Criteria in Regulation 15 is applied to the Connection Capacity or the DSR Capacity. These are un-de-rated figures. In contrast, Rule 9.2.4(a)(ii) compares the Capacity Obligation – a de-rated figure – to that same Minimum Capacity Threshold. Similar mistakes are made throughout Chapters 9 and 13A.

6 Delivery Body, CMU Market CMU transfer guidance v2.0, December 2018.

7 Rather than setting out general conditions for transfers of any CMU, Rule 9.2.4 instead just makes provisions for (b) transfers of Generating CMUs from a legal owner to another legal owner or Despatch Controller, (c) transfers of Generating CMUs from a Despatch Controller to the legal owner, and (d) transfers of Interconnector CMUs.

We would recommend a similar approach, of rewriting based on explicit principles, be taken to other particularly opaque parts of the Rules, such as § 6.10 and Chapter 13A.

Q15 Do you agree that it would be desirable to allow obligations to be traded between parties in amounts greater than or equal to 0.5MW?

Yes. This would also overcome the issue with sub-2 MW CMUs mentioned above.

Q16 Do you believe the current time period of five Working Days before the date of the trade by which applicants must submit a request to trade is appropriate or should this period be reduced? Do you have any suggestions on a revised length of this period?

To minimise barriers to trading, this period should be as short as possible. If the Delivery Body and Settlement Body do not have five days of work to do to process a trade, then it should be reduced. We agree that two working days would seem ample: one day to do the work, and a one day buffer to allow for disruptions.

Q17 Do you believe that the current period of three months in which NGESO have to notify a Secondary Trading Entrant of the Prequalification decision is appropriate or do you feel this should be shortened? Do you have any suggestions on a revised length of this period?

This period should be shortened substantially, as it makes participation as a Secondary Trading Entrant impractical. Since the Delivery Body is currently able to assess over a thousand applications during the six week prequalification assessment window, they must surely be able to assess occasional applications from secondary trading entrants much faster. Two weeks would seem generous.

Q18 Do you agree with adding a provision for the time frame over which NGESO must respond to requests for a trade?

Yes. Maximum times should be established for all steps through all possible paths.

Q19 Do you think it is appropriate to extend the defined trading window to the results day of the T-4 Auction for the relevant Delivery Year?

Yes, for all the reasons given in the consultation paper.

Q22 How should we address the risk of a trade being withdrawn where a Transferor is terminated after a trade has been registered?

In the circumstances described, the transfer should go ahead. It is true that a provider facing termination would seek to trade away the obligation, rather than paying the termination fee. However, we do not see why this would be considered a problem: it is a better outcome for the capacity to be delivered by another party than for the agreement to be terminated.

Q23 How should we address the transfer termination risk where a partial or full Capacity Agreement is traded for part of, or the entire duration of a Delivery Year?

For transfers of part of a Capacity Agreement for a full Delivery Year, it seems obvious that the transferred part should be unaffected by termination of the original CMU. As in the previous question, it is better for the capacity to be delivered by another party than not at all.

From the perspective of the Transferee, this also seems the best approach: otherwise, any Capacity Obligations acquired through secondary trading come with an entirely unpredictable and unmanageable termination risk.

We agree that it is less obvious how best to handle trades for part of a Delivery Year. From the Transferee's perspective, it is the same: they do not want the risk that the capacity will disappear. Perhaps a sensible approach would be to allow the transferor to avoid paying termination fees if they manage to arrange additional secondary trades to cover the rest of the Delivery Year.

Q24 Are there any amendments that could be made to the SPD framework following a secondary trade, specifically relating to partial agreement trades?

We do not believe that anybody actually understands Rule 9.5. It may be, as suggested in ¶ 5.32 of the consultation paper, that it covers all possible trade situations. But there is no way to be sure of this.

Along with the rest of the chapter, it should be re-written from scratch, starting with an explicit declaration of the principles which are meant to apply.

6 Other changes to the Rules

Q25 Do you believe the options presented related to SPD data submission are suitable and are there any options we may not have considered in order to help mitigate the impact on capacity providers?

We agree that the root cause is in the relationship (or lack thereof) between data collectors/aggregators and capacity providers. The suggested actions will help, but

we recommend that there should also be provision for meter data to be accepted via other routes, as a fallback in cases where it proves impossible to fix a data flow issue in time to meet a deadline.

Q26 Which aspects of a CMU configuration do you think should not be able to be amended following Prequalification?

De-rated capacity seems the only truly vital attribute, since that is what the capacity market exists to buy. It is not clear why it would be desirable to prevent any other changes.

Q27 Is there any other data that would be useful to add to the CMR and why?

It is worth noting that many DSR sites use a combination of "turn down" and generation. Any information provision requirement should allow for such hybrid components.

7 NGESO's incentives and role in the CM

Q32 Do NGESO's current financial incentives on demand forecasting accuracy, dispute resolution, DSR Prequalification, and customer and stakeholder satisfaction drive the intended behaviours by NGESO?

As discussed in § 9 of our previous submission, we do not believe that the current financial incentives are effective at driving desirable behaviour from NGESO.

Q33 Do the financial incentives listed above remain fit for purpose?

No. It is not clear that they ever were.

Q34 What behaviours and outcomes should NGESO's financial incentives drive? What form should these incentives take?

The desired behaviour is for NGESO to put significant effort into running an effective market in an efficient manner. They should seek to minimise errors, and to remedy them quickly when they inevitably occur. They should respond quickly and accurately to enquiries. They should use their skill and judgement to overcome ambiguities in a constructive manner. Their main aim should be to make things work, rather to minimise legal risk to NGESO.

We are not experts on financial incentives.

8 Postponed changes

We welcome the implementation of Of12. However, we have a few remaining concerns with the proposed rule, described below. Fortunately, they are simple to fix. We strongly recommend that these fixes are applied, so that Of12 will be effective.

Limits on transfers under Of12

Paragraph 8.6 of the consultation paper mentions Ofgem's welcome decision to raise the annual limits on the number of transfer notifications and the number of affected components. The consultation text does not make clear to what entity those limits are applied.

Our understanding, from separate discussion and correspondence with Ofgem, is that the intention is for the limits to apply to each CMU. Unfortunately, this is not what the proposed drafting of Rule 8.3.4(j) in the appendix says:

> *A Capacity Provider may make a notification pursuant to Rule 8.3.4(e) no more than ten times within a Delivery Year, and must in total add no more than forty new DSR components within one Delivery Year.*

Applying the limit at the level of the Capacity Provider would be illogical: it would mean that larger participants would be able to carry out far fewer transfers per CMU. This would encourage larger participants to split their CMUs between multiple special-purpose companies, so as to reduce the risk of exhausting their transfer quota. It seems perverse to encourage such behaviour.

We therefore recommend that the drafting of Rule 8.3.4(j) be changed to something like this:

> *For each CMU, a notification pursuant to Rule 8.3.4(e) can be made no more than ten times within a Delivery Year, and no more than forty new DSR components can be added within one Delivery Year.*

Timing of transfers under Of12

There is another issue with Of12, which we have raised before, but has not yet been addressed: it does not provide a means for a component to transfer from one CMU to another between Delivery Years. The lack of such a mechanism would frustrate competition between aggregators, as some changes would require the component to "sit out" from the market for a year, which would strongly discourage customers from switching aggregator.

The issue is with the timing of transfers. Specifically:

- Rule 8.3.4(c) says that component removals happen 5 Working Days after receipt of a notification. This can be done at any time.

- Rule 8.3.4(d) says any component that has been removed cannot be added to any CMU for the same Delivery Year.
- Rule 8.3.4(e) says that component additions cannot be notified in the last 2 months of a Delivery Year.
- Rule 8.3.4(g) says that component additions happen 21 Working Days after receipt of a notification.

With these restrictions, there does not seem to be any way for a component to remain in CMU A until the end Delivery Year T, then be in CMU B from the start of Delivery Year T+1, which is what is needed for a customer to be able switch aggregators painlessly.

This can be remedied by allowing component additions and removals to happen on specified dates, rather than just happening automatically a certain number of working days after notification.

This could be implemented in a similar manner to the secondary trading and CMU transfer arrangements, by requiring the specified transfer date to be at least a certain number of working days in the future.[8] The following amendments to the drafting of Rule 8.3.4 might work for this:

(b) *A Capacity Provider may notify the Delivery Body and the CM Settlement Body that it wishes to remove, on a specified date which is at least five Working Days after notification, one or more DSR CMU Component from a DSR CMU that is a Capacity Committed CMU.*

(c) ~~*With effect from the date falling five Working Days*~~ *After receipt by the CM Settlement Body of a notice pursuant to Rule 8.3.4(b), with effect from the specified date: …*

(e) *A Capacity Provider may notify the Delivery Body and the CM Settlement Body~~, during the relevant Delivery Year and no later than two months prior to the subsequent Delivery Year,~~ that it wishes to add one or more DSR CMU Component to a DSR CMU that is a Capacity Committed CMU, with effect from a specified date that is at least twenty-one Working Days after notification, and not within the final two months of the Delivery Year.*

(g) ~~*With effect from the date falling twenty-one Working Days*~~ *After receipt by the CM Settlement Body of a notice pursuant to Rule 8.3.4(e), and only where the conditions of Rule 8.3.4(h) have been met, with effect from the specified date: …*

An even simpler approach would be to allow notifications to be forward-dated only to the start of the next Delivery Year, not to any arbitrary date.

[8] Rule 9.3.1(a).

One important implementation detail is that any DSR Test for the new CMU that is required before the start of the Delivery Year should include the components which are scheduled to be added to the CMU at the start of the Delivery Year. This can be done in Rule 13.2.2(c):

> *where Rules 8.3.4(b) or 8.3.4(e) apply, prior to the commencement of the subsequent Delivery Year, and after the final notification of component additions and/or removals, in which case the CMU should be tested with the components it will have at the start of the subsequent Delivery Year.*

Provision for Joint DSR Tests in Of12

Whereas proposed Rule 13.2.2(c) allows for a DSR Test to be carried out on a CMU to which component changes have been made, there is no equivalent provision for Joint DSR Tests. All that is needed is to add an equivalent clause 13.2B.2(c).

I would be happy to provide further detail on these comments, if that would be helpful.

Yours faithfully,

Dr Paul Troughton
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