

Department of Energy & Climate Change
3 Whitehall Place
London, SW1A2AW
England



Our date: 3rd October 2011

Consultation on possible models for a capacity mechanism

As the Transmission System Operator in Norway and as a partner of National Grid in the interconnector project North Sea Network (NSN), Statnett welcomes the opportunity to participate in DECC's consultation on possible models for a capacity mechanism.

Statnett believes that it's in the interest of Great Britain to facilitate realization of new interconnectors. Combining the flexible Norwegian hydro power system with the GB generation mix will increase the overall efficiency of the two power systems. The NSN interconnector can also contribute to reduce greenhouse gas emissions from the GB electricity market, by enabling more wind power to be introduced in the GB market.

Investing in interconnectors is expensive and involves a significant risk. It's important that a capacity mechanism doesn't remove the incentives for investing in interconnectors, by capping prices or increasing risk. This may otherwise increase total costs for the power system.

Question 1: Does this table capture all of your major concerns with a targeted Capacity Mechanism? Do you think the mitigation approach described will be effective?

In our view the most important concerns are captured in this table. As a potential interconnector investor our major concern is market distortion and reduced incentives for investments, which may also increase total costs in the power system unnecessary. With a strategic reserve, it's important that the reserve affect the electricity price as little as possible to minimize market distortion. In that respect, holding the strategic reserve capacity out of the market is a good idea. The dispatch price level is also important, and we will get back to that in our reply to question six.

Question 5: How can a Strategic Reserve be designed to encourage the cost-effective participation of DSR, storage and other forms of non-generation technologies and approaches?

DSR, storage and other forms of non-generation technologies and approaches should be allowed to participate in a strategic reserve. The Nordic experience from the Swedish strategic reserve is however, that it's a disadvantage that the demand reduction reserves were withheld from the market. For the coming year some changes will therefore be implemented. The most important is that the demand side will be allowed to freely bid into the day-ahead market even when being part of the strategic reserve. This change does not apply to supply side reserves. Allowing them to bid into the day-ahead market is intended to stimulate the development of an active demand side. This may also apply to storage and interconnectors.

Question 6: Government prefers the form of economic despatch described here. Which of the proposed despatch models do you prefer and why?

The level of the despatch price is very important. The despatch price should be significant above the highest long-run marginal cost in the electricity market to minimize market distortion. Otherwise one may risk that for instance demand flexibility is not optimally utilized.

Question 17: How should the reference market for reliability contracts be determined and what would be an appropriate reference market if it is set by the regulator? How could any adverse effects of choosing a particular option be mitigated?

If reliable capacity is not sold in the reference market the providers face the risk of having to pay back more than they earn. Hence, the providers of reliable capacity have an incentive to sell their electricity in the reference market to hedge against the risk of these paybacks. The Framework Guideline on Capacity Allocation and Congestion Management for Electricity and the development of codes may give reduced flexibility for interconnector owners to choose markets for the capacity themselves.

To avoid increased risk for interconnectors, the design of a Reliability Market should take this in to account when deciding on a reference market.

Question 22: How can a Capacity Market be designed to encourage the cost-effective participation of DSR, storage and other non-generation technologies and approaches?

Interconnectors can be competitive participants in a capacity market. During peak-hours flexible Norwegian hydro can be exported and provide GB with more capacity. If such a mechanism is introduced, it will be suboptimal to discriminate against interconnectors.

Yours faithfully
Stagnett SE



Head of Market Design
Commercial Development



Advisor
Commercial Development