

## Consultation on Possible Models for a Capacity Mechanism

### Response form

Responses are welcome by email or post. You may find this document helpful for structuring your response, but can reply in a separate document if you prefer. If replying in a separate document please make clear which questions you are answering.

Respondent Details	
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Tick this box if you are requesting non-disclosure of your response. ☐

Please return by 30 September 2011 to:

Department of Energy & Climate Change,  
Electricity Market Design – Security of Supply  
4th Floor, Area D  
3 Whitehall Place,  
London, SW1A 2AW

You can also submit this form by email to:  
[DECC.capacity.mechanism@decc.gsi.gov.uk](mailto:DECC.capacity.mechanism@decc.gsi.gov.uk)

## Consultation questions

Note: the references in square brackets refer to page and figure numbers in the consultation document where more information can be found, and the questions are set out in context. The consultation document is Annex C of the Electricity Market Reform White Paper, and is available here:

[http://www.decc.gov.uk/en/content/cms/consultations/cap\\_mech/cap\\_mech.aspx](http://www.decc.gov.uk/en/content/cms/consultations/cap_mech/cap_mech.aspx)

### *Targeted mechanism*

Consultation question [page 167]	
<b>1</b>	<b>Does this table [see Figure C3] capture all of your major concerns with a targeted Capacity Mechanism? Do you think the mitigation approach described will be effective?</b>
<b>Response</b>	The mitigations are likely to be too interventionist in this case with high possibilities of unintended consequences. The mitigations will be unnecessary if the System Operator is given, as part of its license, a duty of achieving the objectives of a strategic reserve by 'least cost' means. Complex price setting and related rules in this case is likely to lead to 'gaming' by major electricity companies. The reserve should be termed as being a requirement on the System Operator to provide system reliability which is likely to be achieved by a combination of measures: DSR, interconnection, independent generation, storage, as well as large power plant.

Consultation question [page 168]	
<b>2</b>	<b>How long should the lead time for Strategic Reserve capacity procurement be and why?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 168]	
<b>3</b>	<b>Should the length and nature of contracts procured by the Strategic Reserve procurement function be constrained in any way?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 169]	
<b>4</b>	<b>Which criteria should providers of Strategic Reserve be required to meet?</b>

<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.
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Consultation question [page 169]	
<b>5</b>	<b>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?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. Rules set at this stage through this consultation will not only bind the hands of The System Operator but in all likelihood reflect the interests of major electricity companies who wish to maximise income through generation from large power stations rather than encourage possibilities for options such as DSR, grid inter-connections or independent generation.

Consultation question [page 175]	
<b>6</b>	<b>Government prefers the form of economic despatch described here. Which of the proposed despatch models do you prefer and why?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 175]	
<b>7</b>	<b>How would the Strategic Reserve methodology and despatch price best be kept independent from short-term pressures?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 175]	
<b>8</b>	<b>Do you agree that a Strategic Reserve should be periodically reviewed? If so, who would be best placed to carry out the review and how often should it be reviewed?</b>
<b>Response</b>	Yes, arrangements should be periodically reviewed. This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 176]	
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<b>9</b>	<b>Into which market should Strategic Reserve be sold and why?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 178]	
<b>10</b>	<b>Do you have any comments on the functional arrangements proposed for managing a Strategic Reserve?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 179]	
<b>11</b>	<b>Given the design proposed here and your answers to the above questions, do you think a Strategic Reserve is a workable model of Capacity Mechanism for the GB market?</b>
<b>Response</b>	In general, yes, but the details should not be decided in this review, and should certainly not be set 'on the face' of Parliamentary legislation. As stated in answer to Question 1, the System Operator should be given, as part of its license, a duty of achieving the objectives of a strategic reserve by 'least cost' means. Complex price setting and related rules in this case is likely to lead to 'gaming' by major electricity companies.

### *Market-wide mechanism*

Consultation question [page 182]	
<b>12</b>	<b>How and by whom should capacity in a GB market be bought and why?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 183]	
<b>13</b>	<b>What contract durations would you recommend for a Capacity Market?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 184]	
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<b>14</b>	<b>How long should the lead time for capacity procurement be? Should there be special arrangements for plant with long construction times?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

<b>Consultation question</b>		<b>[page 185]</b>
<b>15</b>	<b>Should there be a secondary market for capacity? Should there be any restrictions on participants or products traded?</b>	
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.	

<b>Consultation question</b>		<b>[page 186]</b>
<b>16</b>	<b>What are the advantages and disadvantages of making a central, administrative determination of (i) the capacity that can be offered into the market by each generator; (ii) the criteria for being available; and (iii) the penalties for non-availability? In outline, how would you suggest making these determinations?</b>	
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.	

<b>Consultation question</b>		<b>[page 191]</b>
<b>17</b>	<b>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?</b>	
<b>Response</b>	As argued earlier, the added complexities of interventionist price setting should be avoided (except when necessary for specific technological targeting, eg for renewable energy technologies). The System Operator needs to be given the flexibility to establish and where necessary, amend, strategic market reserve structures to meet its own duty of achieving security of supply by least cost means. It should perform this duty in the context of discussions with the Regulator.	

<b>Consultation question</b>		<b>[page 192]</b>
<b>18</b>	<b>For a Reliability Market, how should the strike price be determined? If using an indexed strike price, which index should be used?</b>	



<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.
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Consultation question [page 193]	
<b>19</b>	<b>For a Reliability Market, what level of physical back up (if any) should be required for reliability contracts and how should it be monitored?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 194]	
<b>20</b>	<b>Do you agree that a vertically integrated market potentially raises issues for the effectiveness of a Reliability Market? If so, how should these issues be addressed?</b>
<b>Response</b>	Yes, the power of the 'big six' certainly does raise issues. This is why it is so necessary to give the authority and duty to achieve general objectives to the System Operator. They are in the best position to judge how security of supply can be achieved through least cost means since they are independent of those offering strategic reserve resources. The more we set complex rules, the more opportunity there will be for the major electricity companies to earn economic rents.

Consultation question [page 195]	
<b>21</b>	<b>What could we do to mitigate interactions between a Capacity Market (especially if a Reliability Market) and Feed-in Tariff with Contract for Difference without diluting the effectiveness of either?</b>
<b>Response</b>	The contract for differences feed-in tariffs themselves introduce too many unnecessary complexities that would not occur with simpler so-called 'fixed' feed-in tariffs. Establishing a capacity market with predetermined complex rules would exacerbate the situation further and leave the system to be manipulated to a considerable extent by major electricity companies. The rules for a 'reliability market' are a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 196]	
<b>22</b>	<b>How can a Capacity Market be designed to encourage the cost-effective participation of DSR, storage and other non-generation technologies and approaches?</b>

<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.
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Consultation question [page 199]	
<b>23</b>	<b>Do you have any comments on the functional arrangements proposed for managing a Capacity Market?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 199]	
<b>24</b>	<b>Do you think that a trigger should be set for the introduction of a Capacity Market? If so, how do you think the trigger should be established, and how should it be activated?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Consultation question [page 199]	
<b>25</b>	<b>What is the most appropriate design of Capacity Market for GB and why?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

### *Capacity mechanism Assessment*

Consultation question [page 210]	
<b>26</b>	<b>What are your views on the costs and benefits of a Capacity Mechanism to industry and consumers?</b>
<b>Response</b>	As rational choice theory suggests, this depends on the perceived self-interest of the actors making the decisions. If matters are left to the System Operator, with a duty to achieve security of supply by least cost means, then the benefits of a reliability arrangements (including DSR, independent generation, storage, interconnection) are considerable. A 'capacity' market overseen by a series of complex pre-determined rules is only likely to benefit the major electricity companies, not consumers whether industrial, commercial or residential.

27	<b>Which Capacity Mechanism should the Government choose for the GB market and why?</b>
<b>Response</b>	This is a matter for the System Operator to discuss in consultation with the Regulator. See response to Question 1.

Please select the category below which best describes who you are responding on behalf of.

- ☐ Business representative organisation/trade body
- ☐ Central Government
- ☐ Charity or social enterprise
- ☐ Individual
- ☐ Large business ( over 250 staff)
- ☐ Legal representative
- ☐ Local Government
- ☐ Medium business (50 to 250 staff)
- ☐ Small business (10 to 49 staff)
- ☐ Micro business (up to 9 staff)
- ☐ Trade union or staff association
- ☒ Other (please describe): Academic

Thank you for taking the time to let us have your views.

The Government does not intend to acknowledge receipt of individual responses unless you tick this box. ☐