EXPLANATORY MEMORANDUM TO

THE ELECTRICITY CAPACITY (AMENDMENT) REGULATIONS 2023

2023 No. 860

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Energy Security & Net Zero and is laid before Parliament by Command of His Majesty.

2. Purpose of the instrument

2.1 This instrument amends the Electricity Capacity Regulations 2014 (S.I. 2014/2043) in order to make technical amendments to the Capacity Market (CM) aimed at better enabling existing provisions to be used in practise, reducing administrative burdens, and improving administrative arrangements for the CM.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

4. Extent and Territorial Application

4.1 The extent of this instrument Great Britain.

4.2 The territorial application of this instrument Great Britain.

5. European Convention on Human Rights

5.1 The Minister of State for the Department for Energy Security & Net Zero, Minister Stuart, has made the following statement regarding Human Rights:

"In my view the provisions of the Electricity Capacity (Amendment) Regulations 2023 are compatible with the Convention rights."

6. Legislative Context

6.1 Chapter 3 of Part 2 of the Energy Act 2013 (the Act) provides the Secretary of State powers to make electricity capacity regulations for the purpose of providing capacity to meet consumer demand for the supply of electricity in Great Britain.

6.2 This instrument amends the Electricity Capacity Regulations 2014.

7. Policy background

What is being done and why?

7.1 The CM is at heart of the Government's arrangement for maintaining a secure and reliable electricity system. The CM provides all forms of electricity capacity capable of contributing to security of supply with the right incentives to be on a system and to deliver during periods of electricity system shortage and stress, for example during cold, still periods where demand is high and wind generation is low. This includes traditional technologies, such as gas-fired generation and nuclear, as well as intermittent renewables (e.g., wind and solar), demand side response (DSR) which

delivers capacity by reducing demand, storage assets and interconnection with other countries.

7.2 The CM works by allowing eligible bidders to compete in auctions – either four years ("T- 4 auction") or one year ("T-1 auction") ahead of when they must deliver capacity. Auction bids are made by Capacity Market Units (CMUs) – the unit of generation, interconnection, or DSR in respect of which a capacity agreement is awarded. Successful bidders ("Capacity Providers") are awarded capacity agreements which oblige them to deliver capacity (by generating electricity or in the case of DSR CMUs, reducing demand) at times of system stress. They face financial penalties if they fail to deliver. They receive capacity payments, which incentivise the necessary investment to maintain and refurbish capacity, and to finance new build capacity. The large majority of CM agreements are one-year in duration, but agreements of up to fifteen years are available to certain new build projects and up to three years for certain refurbishing projects, to support investment.

7.3 This instrument makes changes to three regulations in the Electricity Capacity Regulations 2014.

7.4 Amendment to regulation 10: Requirement for the Secretary of State to determine whether the capacity auctions are to be held: Regulation 10 sets out the obligation on the Secretary of State to decide whether capacity auctions are to be held. Regulation 10(5) requires those determinations to be published. This instrument will remove references to past auctions that have already been held as these references are no longer required. This instrument also amends regulation 10(5) to only require the Secretary of State to publish a decision if they determine that a T-1 or T-4 auction (or both) will not be held, to reflect that the CM is a well-established mechanism that has been operating for several years and this will increase administrative efficiency.

7.5 Amendment to regulation 34: Termination of capacity agreements to enable applications to the CFD scheme: Regulation 34 allows Capacity Providers to seek termination of their capacity agreement with a view to becoming eligible to participate in the Contracts for Difference (CFD) scheme. The CFD scheme is the Government's main mechanism for supporting low-carbon electricity generation. This termination is made possible in theory by the Delivery Body of the CM terminating a capacity agreement where a "CfD transfer notice" has been received in relation to the Capacity Provider's CMU. Regulation 34(3) provides that the "CfD transfer notice" comes from the CFD Counterparty (the Low Carbon Contracts Company or LCCC) and states that LCCC intends to grant a CfD to the CMU. However, in practice, LCCC can never know in advance that the CMU in question will be successful in an application in a CfD allocation round. This means that LCCC cannot provide a Capacity Provider with a "CFD transfer notice". This has meant that eligible Capacity Providers are unable to use the process set out in regulation 34. This instrument amends the definition of "CfD transfer notice" so that it comes from a Capacity Provider who seeks the termination of their capacity agreement in order to become eligible to apply in a CFD allocation round. More information about the Contract for Difference scheme is available here https://www.gov.uk/government/publications/contracts-for-difference/contract-for-difference

7.6 Amendment to regulation 41: Timeline for calculating non-delivery penalties: Capacity Providers can be financially penalised if they do not deliver capacity in times of system stress. Currently, regulation 41 provides that the Settlement Body for the CM (the Electricity Settlements Company) has 21 working days to calculate the

relevant penalty and invoice Capacity Providers who must pay such penalties. This instrument makes a minor change to increase that time period to 35 working days. This is to ensure that the Settlement Body has sufficient time to receive relevant data so it can accurately calculate penalties for Capacity Providers and issue the associated invoices.

8. European Union Withdrawal and Future Relationship

8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act

9. Consolidation

9.1 There are no plans to consolidate the legislation amended by the instrument.

10. Consultation outcome

10.1 A public consultation was conducted in relation to the measures in this instrument. A Government Response, including a summary of consultation responses, was published on 12 June 2023 and is available here: https://www.gov.uk/government/consultations/capacity-market-consultation-strengthening-security-of-supply-and-alignment-with-net-zero.

10.2 The consultation was conducted between 9 January 2023 and 3 March 2023 and sought a range of views on a range of proposals related to the CM. 65 responses were received from a variety of stakeholders, including capacity providers and trade associations. Respondents were broadly supportive of the proposals included in this instrument.

10.3 In regards to changes to regulation 10, a few responses felt that current timelines for a Secretary of State announcement should be maintained to inform business decisions. As noted in the response to consultation, the legislative changes will be made to require Secretary of State to publish a decision if a T-1 or T-4 auction (or both) will not be held but the Government intends to maintain the associated timescales for that. In regards to changes to regulation 41, some broader feedback was shared by respondents on wider system improvements to the penalties framework, rather than the specific change implemented in this instrument. A response to the more general comments on the penalties framework in the CM is addressed in the response to the consultation. A few objections were raised by respondents to the proposed amendments to regulation 34, which facilitates the termination of capacity agreements to enable applications to the CFD scheme. The Government has addressed these objections in the response to the consultation, noting that the change being made is intended to make appropriate amendments to enable an existing transfer route to be used in practise, but that the Government intends to monitor the impacts of this change to ensure continued alignment with the core objectives of the CM.

11. Guidance

1.1 Guidance on the CM is produced by the Delivery Body and the Electricity Settlements Company Ltd is published on their websites and is available here:
https://www.emrdeliverybody.com/cm/home.aspx
https://www.emrsettlement.co.uk/publications/guidance/

11.1 Guidance on how the changes made to this instrument will impact the CM will be published by the Delivery Body, if necessary.

12. Impact

12.1 There is no, or no significant, impact on business, charities, or voluntary bodies.

12.2 There is no impact on the public sector.

12.3 An Impact Assessment has not been prepared for this instrument because this instrument relates to the maintenance of the CM and is administrative in nature. This instrument is intended to better enable existing frameworks to be used in practise and improve existing administrative arrangements for the delivery of the CM and as such the impact on businesses is small and no impact is foreseen on the voluntary or public sector. The CM was subject to a full Impact Assessment when it was first introduced.

13. Regulating small business

13.1 The legislation applies to activities that are undertaken by small businesses.

13.2 No specific action is proposed to minimise regulatory burdens on small businesses. It is anticipated that due to the technical and administrative nature of the changes, any impacts on small businesses would be small.

14. Monitoring & review

14.1 The provisions of the Act which underpin the CM are required (by section 66 of the Act) to be reviewed every five years and regulation 81 of the Electricity Capacity Regulations 2014 requires a five-yearly review. The first five-year review was published 22 July 2019. The review found that the CM performance against its objectives has been good. The review did not recommend major changes but identified incremental improvements which the Government will implement in due course. The second five year review of the CM will be published in 2024, and the amendments made by this instrument will be in scope of it.

15. Contact

15.1 Luke Nightingale at the Department for Energy Security & Net Zero Telephone: +442072151440 or email:luke.nightingale@beis.gov.uk can be contacted with any queries regarding the instrument.

15.2 Simon Masterson Deputy, Director for Energy Security Markets and Analysis, at the Department for Energy Security & Net Zero can confirm that this Explanatory Memorandum meets the required standard.

15.3 Minister Graham Stuart at the Department for Energy Security & Net Zero can confirm that this Explanatory Memorandum meets the required standard.