Electricity & Market Arrangements
Capacity Market Team
Department for Energy Security and Net Zero
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To whom it may concern,

Consultation Response: Capacity Market 2023 – Phase 2 proposals and 10 year review

Scottish Renewables is the voice of Scotland's renewable energy industry. Our vision is for Scotland leading the world in renewable energy. We work to grow Scotland's renewable energy sector and sustain its position at the forefront of the global clean energy industry. We represent over 340 organisations that deliver investment, jobs, social benefits and reduce the carbon emissions which cause climate change.

Our members work across all renewable energy technologies, in Scotland, the UK, Europe and around the world. In representing them, we aim to lead and inform the debate on how the growth of renewable energy can help sustainably heat and power Scotland's homes and businesses.

Scottish Renewables also convenes the UK Pumped Storage Hydro working group which comprises developers including SSE Renewables, Drax Power, ILI Group, Buccleuch, Foresight, Dorothea Pumped Hydro, Gilkes Energy, CCSQ as well as the British Hydropower Association. Our members currently have a combined pipeline of over 7GW of new pumped storage hydro (PSH) projects with over 135GWh of storage capacity.

Response to Capacity Market Phase 2 proposals

<u>Projects with long build times</u>

In responding to the Phase 1 consultation earlier this year, Scottish Renewables highlighted the need to allow long build time projects such as PSH to participate in the Capacity Market

(CM). With suitable eligibility and operational conditions in place to minimise the risks and uncertainties of non-delivery, Scottish Renewables is supportive of proposals to allow long build time projects to compete in T-4 auctions. We therefore welcome that government has considered measures to this effect.

However, we do not believe that the additional 24-month longstop date will be sufficient to allow new build large-scale PSH projects to participate in T-4 auctions. It is our understanding that the additional 24-month longstop date will allow projects less than six years to complete construction and begin commercial operation. Given the size and complexities of PSH projects as well as the uncertainties associated with large tunnelling and excavation activities due to unknown ground conditions, this is unlikely to be sufficient.

Additionally, given that PSH projects have very high CapEx as well as long build times, the full 15-year contract length is critical for projects seeking project finance. Any significant reduction in the contract length would likely prevent PSH projects from securing enough financing as they will be unable to pay back the debt over this reduced period. Scottish Renewables therefore believes that a minimum of a 36-month extension or delay to delivery rather than the proposed additional 24-month longstop date will be required to allow these projects to participate.

In seeking to allow long build time projects to participate in T-4 auctions, it is also crucially important that government sets out in detail how the auction will be adapted to minimise any risks of distortion. As per our response to the Phase 1 consultation, Scottish Renewables believes that there is merit in allowing long build time projects to participate directly in the auction but with their capacity treated as a nominal capacity (e.g., sub 1MW). This would ensure that the unit can take part in price discovery but not undermine security of supply in the T-4 delivery year.

Finally, Scottish Renewables would urge the government to provide clarification of how access to long-term CM agreements may be impacted by the implementation of an adapted Cap and Floor mechanism for large-scale, long duration electricity storage (LLES). As we have emphasised in our response to the Phase 1 consultation and others, both an adapted Cap and Floor mechanism and a reformed CM are critical to enabling the deployment of LLES projects.

Capacity Market and Contracts for Difference participation

We support the proposal to clarify the regulations concerning non-permitted CM and CfD participation. However, we ask that the wording is further developed to provide clarity to generators.

We would ask for further clarity from the EMR Delivery Body that generators which have already been subject to the CfD can then enter the CM as Existing units after their CfD agreement expires (at the end of the 15-year period).

Further, termination and expiration are not the only eventualities existing under the CfD, which also allows for reduction of capacity in some instances. Further clarity is required to remove barriers to participation for renewable generation that does not receive a subsidy but may be captured by the current limited wording.

Battery degradation

We support the proposals to help address barriers faced by storage CMUs in managing battery degradation.

We encourage DESNZ to consider additional proposals in future which could provide further improvements, such as the use of a capacity degradation profile for battery storage. We believe the Rules would need to be aligned with the current arrangements for Satisfactory Performance Days. For example, secondary trades would need to cover the entire Delivery Year to qualify, and the EPT would need to be retaken the following year if the CMU was no longer subject to a secondary trade.

Governance arrangements

The prequalification process remains difficult to navigate for new entrants and the screening of applications leaves zero room for error. This means that many applications are rejected during the first stage, which incurs a dispute process and ultimately an inefficient use of resources for both applicant and the EMR Delivery Body. We urge that the prequalification screening process is updated to limit inefficiencies.

Further comments

We support the proposals to relating to further aligning Regulation 50 with policy intent, introducing 9-year agreements, and amending the Extended Years Criteria.

Response to 10 year Review - flexibility

We welcome that a fundamental review of the CM is being undertaken alongside REMA. In our prior REMA response, we highlighted the market reforms we consider are needed to deliver an efficient, secure, low carbon electricity market. Of these, flexibility is critical for a net-zero energy system and, to enable investment in flexibility resources, we suggest that REMA and CM reform needs to address the following issues:

- **Defining flexible capacity targets** – we suggest these should include dispatchable generation or demand, plus dispatchable ancillary services such as inertia, plus network congestion flexibility. It should prioritise low-carbon flexibility.
- **Valuing flexibility** – long term price signals for flexibility are not being provided by existing capacity, wholesale or balancing markets. Short-term flexibility market prices are incentivising short duration storage which in turn is cannibalising revenues from lower long-run cost flexibility solutions.

Scottish Renewables would be keen to engage further with this agenda and would be happy to discuss our response in more detail.

Yours sincerely,

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