



EnergyAustralia

LIGHT THE WAY

6 February 2018

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Dear Commissioners

Lodged electronically: www.aemc.gov.au (EPR0060)

AEMC, Reliability Frameworks Review, Interim Report, 19 December 2017

EnergyAustralia is one of Australia's largest energy companies with over 2.6 million electricity and gas accounts in NSW, Victoria, Queensland, South Australia, and the Australian Capital Territory. We also own and operate a multi-billion dollar energy generation portfolio across Australia, including coal, gas, and wind assets with control of over 4,500MW of generation in the National Electricity Market (NEM).

EnergyAustralia welcomes the opportunity to further comment on the Reliability Frameworks Review (Review). We consider that the Interim Report (Report) provides a useful starting point for identifying key challenges affecting the NEM. Overall, we consider the Report sets out a thorough examination of key factors impacting reliability.

We note that the Report has deferred specific consideration of the interaction between possible reliability framework amendments and the proposed National Energy Guarantee (NEG) to the Directions Paper. Given the inherent relationship between the reliability framework and the reliability component in the NEG, we consider integration of the interactions between the policies is essential. Key issues, regarding the integration of the NEG, to be considered for the Directions Paper are highlighted in our below feedback on the Interim Report.

Forecasting

EnergyAustralia strongly supports the focus on improving the accuracy of forecasting demand for electricity in the NEM, as accurate forecasts are a key driver of reliability. We previously supported a proposed rule change to require increased participation in AEMO's NEM scheduling by smaller generating units as well as larger market loads.¹ Noting that this rule change was not made by the Commission we support further consideration on how the increasing number of smaller individual generating units, aggregated distributed generators and demand response should be managed by AEMO, and how a reduced level of scheduled generation will impact AEMO's ability to operate the NEM reliably.

¹ AEMC Final Determination, ERC0203, Non-scheduled load and generation in central dispatch

The Report suggests that one option for improving forecasting where there is higher demand side participation would be for retailers to have responsibility for forecasting. As highlighted by the Report, this would entail significant costs. Given the decision not to proceed with the proposed rule change on central dispatch, we suggest that further consideration of retailer-led forecasting would need to revisit the outcomes of that rule change and how central dispatch would work as traditionally scheduled generation becomes less significant to market outcomes.

The contract market

We support the initial findings by the Commission that there has not been a substantial reduction of liquidity in the contract market due to the changing generation mix in the NEM. The contract market is an effective driver of reliability, and the flexibility of the market allows participants to develop the appropriate contract positions and products to adapt to changing market conditions.

In our view, the financial contract market has been highly effective in competing down wholesale prices during periods of excess supply. For example, the price of caps has been competed down to \$3-5/MWh in some jurisdictions for extended periods, well below new entrant costs of \$10-15/MWh. This is appropriate and expected in a period of oversupply.

However, in a different market context where policy may seek to incentivise capacity to stay or enter the market, the purely financial nature of the current market may need to be bolstered with some physical checks and balances. For example, if a probabilistic target for demand under reliability settings is adopted in the NEG as a compliance target, then retailers may be required to demonstrate compliance to a low probability of exceedance demand.

Using an extreme example, if retailers were required to demonstrate compliance to a 1 in 100 year demand then capacity prices should trade to the level required to ensure the supply is available for this requirement. However, in a market where the actual observation occurs infrequently, the incentive for financial players is to short the electricity contract and prosper 99 years out of 100. This will then threaten the viability of the capacity required – hence the need to consider physical checks and balances that ensure customers ultimately get electrons from electricity markets.

Any physical checks and balances should be light touch in nature; the financial contract market works well for price competition and the financial market should remain as the cornerstone of trading. Physical checks and balances could be as simple as testing sales are backed by generation (even on an ex post basis). Further work is needed to consider the alternatives and design a fit-for-purpose solution.

Contracting and large customers

The contract market has been highly effective in providing price signals to commercial and industrial users of electricity, informing their choices regarding energy purchasing. Some customers have even chosen not to contract and instead become a spot market consumer of electricity.

The choice to purchase spot electricity indicates a willingness for a commercial and industrial customer to take choices about electricity. Clearly, buying electricity at the market price cap of \$14,200/MWh is expensive and not viable for any business for any large period of time. Therefore, it is reasonable to assume that some customers who choose to purchase off the spot market (or indeed participate in demand response) would prefer not to pay for firm capacity.

In the context of the NEG, this then suggests that these customers (practically, they need to be of a certain size) should have a choice on reliability contracting. If a large customer does not want to pay for firm supply then the market should not build firm capacity for the customer.

In aggregate, we believe the market should see the choices made by large customers in this regard as it will inform the choices to be made by market participants on procuring capacity. We suggest further consideration should be given to explore this issue further by the Commission.

Wholesale Demand Response

EnergyAustralia agrees with the Commission's preliminary view that there are no regulatory barriers to wholesale demand response. We support assessment of whether this may continue to be the case under the proposed NEG. While we agree that there are some issues around the transparency of demand response within the market, we note there are mechanisms in place, or being developed, to assist AEMO with visibility in this area including the demand side participation information guidelines² and register of distributed energy resources³.

We support the ongoing development of processes to improve the transparency of demand response within the NEM. However, we also consider that any assessment of new approaches to providing this must consider the potentially commercially-sensitive nature of the demand response capabilities of commercial and industrial entities. Any transparency measures should avoid acting as a barrier to more large customers participating in demand response. We would recommend that further consultation occur with such customers to understand the impacts of increased reporting on demand response capabilities.

Strategic reserve/RERT

We note that the design of a strategic reserve as an improvement over the current reliability and emergency reserve trader (RERT) mechanism is currently being considered by AEMO, and we support improvements to the current RERT process. Improvements to the contracting process may increase participation and competition in the provision of reserves and hence improve availability and reduce costs. In considering the design of a strategic reserve, or expanded RERT, the need for this mechanism to effectively integrate with any reliability obligation in the NEG must be considered.

² http://www.aemo.com.au/-/media/Files/Stakeholder_Consultation/Consultations/Electricity_Consultations/2017/DSPIG/Demand-Side-Participation-Information-Guidelines.pdf

³ AEMC pending Rule change, ERC0227, <http://www.aemc.gov.au/Rule-Changes/Register-of-distributed-energy-resources>

Day-ahead markets

The section in the Report on day-ahead markets highlights the variety of possible day-ahead market designs, as well as the potential issues that exist in transplanting them into the NEM. Significant alterations to the current NEM would be required, incurring very substantial costs, without there being a clear idea of the merits these changes have in comparison to amendments to the current energy-only design of the NEM. In terms of this Review, we consider that further assessment of a day-ahead market, given the lack of a defined solution it brings and potential scope of impacts, should occur as a separate review that takes into account improvements to the NEM based on the outcome of this Review and associated rule changes.

If you would like to discuss this submission please contact Chris Streets on 03 8628 1393 or at chris.streets@energyaustralia.com.au.

Regards

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