

24 July 2018

John Pierce
Chairman
Australian Energy Market Commission (AEMC)
PO Box A2449
Sydney South NSW 1235

By online submission

Dear Mr Pierce

Enhancement to the Reliability and Emergency Reserve Trader - ERC0237

Hydro Tasmania appreciates the opportunity to provide a response to the Enhancement to the Reliability and Emergency Reserve Trader (RERT) rule change.

This rule change is being considered at a time when the National Energy Market (NEM) is undergoing unprecedented transformation, through both a changing generation mix, and changing market frameworks. There are also a number of reviews either recently completed or underway which are likely to have an influence on the functioning of the electricity market including the development of the National Energy Guarantee (NEG).

It is integral that consideration is given to how the proposed rule change will interact with NEG design including primarily the 'Procurer of Last Resort' function. The Energy Security Board's (ESB) Draft Detailed Design of the NEG states that *'It is not the intention of the Guarantee for AEMO to become the default procurer of capacity for the NEM.'* We are supportive of this statement as this indicates that the intent of NEG design is to incentivise a market response to forecast supply shortfalls in the first instance. To support this intention, we propose that the below principles should guide the development of an appropriate reserve mechanism. Hydro Tasmania considers that reserves should be:

1. an **absolute last-resort** response to maintain reliability and/or system security;
2. designed to **avoid crowding out investment and/or market response**;
3. **activated rarely**;
4. offered by **truly additional capacity only** (must be 'out of market' reserves);
5. **transparent** in nature (with a clearly understood process for procurement, enactment and timely publication of RERT outcomes); and
6. administered at the **lowest-possible cost**.

The Enhanced RERT must meet these principles if it is to function as an appropriate and enduring mechanism. While the proposed mechanism does appear to meet a number of these principles, there are some aspects of the proposed rule change that Hydro Tasmania believes may be at risk of breaching these principles. As such, we encourage the AEMC to consider the following points:

- Hydro Tasmania notes that transparency is a key component of a well-functioning market that underpins information disclosure and investment decisions. Hydro Tasmania encourages consideration of all reasonable opportunities to enhance transparency around the operation of the RERT (without compromising commercially sensitive information). This includes:
 - **Frameworks for procurement and enactment** – At present, there is limited visibility of AEMO’s process for the procurement and enactment of the RERT. Hydro Tasmania understands that consideration is being given to the development of a framework to guide efficient procurement under the RERT, with an ex-post enactment review. These initiatives have the potential to substantially improve transparency on the RERT’s operation, as well as provide insight that may identify opportunities for greater efficiencies. Hydro Tasmania looks forward to providing input to the development of this framework in due course.
 - **Indication of costs** – Hydro Tasmania proposes that a potentially valuable feature that could form part of the Enhanced RERT is for liable entities to be given an indication of the forthcoming costs associated with the scheme. This would allow market participants a clearer understanding of potential forthcoming costs and will assist in budgeting and planning processes.
 - **Apportionment of costs under the NEG** – The NEG’s procurer of last resort function proposes to allow AEMO to procure out of market reserves through the RERT to address periods of forecast supply shortages. It remains unclear how the costs associated with the procurement of the RERT will be applied between compliant and non-compliant retailers under the NEG. We consider it appropriate that any penalties imposed on non-compliant retailers should be utilised to minimise the cost burden of compliant parties. A clear process indicating how costs will be apportioned under the NEG should be developed in consultation with market participants. This will ensure that the operation of the enhanced RERT is well understood in the context of current and proposed market frameworks.
- Hydro Tasmania is concerned with the proposal to allow contracting for RERT over a three year period. This proposal has been put forward by AEMO on the basis that this ‘... *may further increase the number of providers available for reserve contracts and lower the cost of reserves.*’ While we can appreciate the motivation for this proposed amendment to the RERT, we consider that this may produce undesirable market outcomes. For example, in the event that a longer-term ‘gap’ is forecast, the market should be offered every opportunity to respond to that shortfall, before intervention becomes the preferred remedy. We feel this is beneficial as it preserves investment signals. Allowing RERT to be contracted for up to three years could impede market responses and may therefore undermine investor confidence. This would be a suboptimal outcome for the NEM, and would work in opposition to the objectives of the NEG.

Hydro Tasmania looks forward to ongoing engagement with the AEMC. If you would like further information on any aspect of this submission, please contact John Cooper (john.cooper@hydro.com.au or (03) 6230 5313).

Yours sincerely



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