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**EnergyAustralia**

LIGHT THE WAY

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Dear Commissioners,

### **AEMC 2018, Enhancement to the Reliability and Emergency Reserve Trader, Options Paper**

EnergyAustralia is one of Australia's largest energy companies with around 2.6 million electricity and gas accounts in NSW, Victoria, Queensland, South Australia, and the Australian Capital Territory. We also own, operate and contract an energy generation portfolio across Australia, including coal, gas, battery storage, demand response, solar and wind assets with control of over 4,500MW of generation in the National Electricity Market (NEM).

We welcome the opportunity to comment on the AEMC's options paper on AEMO's rule change request Enhancement to the Reliability and Emergency Reserve Trader (RERT).

AEMO remains concerned that the reliability standard may no longer be appropriate given changing system conditions and expectations that consumers and governments are unwilling to tolerate load shedding.<sup>1</sup> AEMO has proposed to delink the RERT framework from the current reliability standard and to move to a broader economic risk assessment framework including creating a standing reserve.<sup>2</sup> AEMO considers this approach would lead to a more stable investment environment that provides greater certainty to developers of resources as well as reducing the risk of load shedding.<sup>3</sup>

EnergyAustralia does not agree that there is a need to change the reliability standard or delink the RERT from this. The Reliability Panel determined only in April 2018 that there was no need for a change to the reliability standard. It also found that any tightening of the standard would come at a significant cost to the consumer.<sup>4</sup> The Reliability Panel, in their response to AEMO's Enhanced RERT rule change, also did not recommend that the

<sup>1</sup> AEMC Option paper, page 25, <https://www.aemc.gov.au/sites/default/files/2018-10/Options%20paper.pdf>

<sup>2</sup> AEMO Additional information to support Enhanced RERT rule change proposal, page 3, <https://www.aemc.gov.au/sites/default/files/2018-11/Additional%20information%20from%20AEMO%20to%20support%20its%20Enhanced%20RERT%20rule%20change%20proposal.pdf>

<sup>3</sup> Ibid., page 3

<sup>4</sup> The reliability standard review found that to improve the USE to 0% in Victoria the cost to consumers would be in the order of \$200-600 million per year. While AEMO is not attempting to achieve 0% USE, they are taking decisions that have the potential to reach this cost level or beyond. <https://www.aemc.gov.au/sites/default/files/2018-04/Reliability%20Panel%20Final%20Report.pdf>

RERT procurement trigger be delinked from the reliability standard.<sup>5</sup> We do not share AEMO's view that delinking the RERT from the current reliability standard and creating a standing reserve will provide a more stable investment environment. Any standing reserve will significantly distort market signals by providing an out of market capacity payment and further remove resources from the market. EnergyAustralia remains concerned by AEMO's comments<sup>6</sup> around the need to provide income certainty to participants in the RERT market and its inability to sign longer term contracts. The RERT is a last resort mechanism. Procuring standing reserve does not give the market sufficient time to provide a market response to any Low Reserve Conditions (LRC) identified and, in fact, may preclude the opportunity for any market response.

### **Appropriateness of the reliability standard**

EnergyAustralia recognises that the NEM generation mix is rapidly changing as older traditional generation is retired and replaced more commonly by variable renewable generation. The NEM has also moved, in just a few years, from having a significant oversupply of generation capacity to a much more balanced supply and demand outlook.

EnergyAustralia does not support AEMO's view that the current reliability framework is not suited to deal with an increasingly 'peaky' demand profile.<sup>7</sup> We agree with the AEMC that the reliability standard does already take into account an increasingly 'peaky' supply-demand balance.<sup>8</sup> This is because AEMO operationalises the reliability standard through the Projected Assessment of System Adequacy (PASA)<sup>9</sup> which carries out numerous simulations of the power system. These simulations use varying forecasts for supply and demand with an increasingly 'peaky' supply-demand balance captured as part of this.<sup>10</sup> Increased peakiness could be expected to result in increased Unserved Energy (USE) which may result in the reliability standard not being met and RERT procurement being undertaken by AEMO. As such, we consider that the reliability standard remains appropriate.

AEMO has proposed, under an economic framework, that it would progressively purchase RERT until a point is reached where the cost of reserve contracts is greater than the value of USE. AEMO argues that linking the RERT to the current standard does not lead to an economically optimal level of reliability as, at times, reserves with costs below that of USE will not be contracted. However, EnergyAustralia does not believe that AEMO has considered the indirect distortionary effects that the RERT can have on market outcomes. There is currently significant focus on increasing the participation of demand response in the market, for example there are several rule change requests currently with the AEMC.<sup>11</sup> The changes proposed by AEMO appear contrary to this and in fact would encourage resources out of the market to participate in the RERT. While at times there may be economic resources that are not utilised (as oppose to potential USE) it is

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<sup>5</sup> Reliability Panel advice on the Enhancement to the RERT rule change, page 6, <https://www.aemc.gov.au/sites/default/files/2018-10/Letter%20of%20Advice%20from%20the%20Reliability%20Panel.pdf>

<sup>6</sup> AEMO Additional information to support Enhanced RERT rule change proposal, page 29

<https://www.aemc.gov.au/sites/default/files/2018-11/Additional%20information%20from%20AEMO%20to%20support%20its%20Enhanced%20RERT%20rule%20change%20proposal.pdf>

<sup>7</sup>Ibid., page 2

<sup>8</sup> AEMC Options Paper, page 26, <https://www.aemc.gov.au/sites/default/files/2018-10/Options%20paper.pdf>

<sup>9</sup> AEMO operationalises the reliability standard in line with its Reliability Standard Implementation Guideline (RSIG), <https://www.aemo.com.au/Stakeholder-Consultation/Consultations/Reliability-Standard-Implementation-Guidelines>

<sup>10</sup> For example AEMO uses both 10% POE and 50% POE traces of demand

<sup>11</sup> <https://www.aemc.gov.au/our-work/changing-energy-rules/rule-changes>

important to recognise that the enduring least cost solution for consumers is to have resource participation through the market and not through the RERT.

Governments are strongly focused on reducing energy costs. Further, consumers have continued to indicate that they are not willing to pay more for a higher level of reliability and appear willing to accept some risk of USE. This is contrary to AEMO's view (with no provided evidence) that government and consumers expectations have shifted, expecting and being willing to pay for a higher level of reliability. Any tightening of the level of the reliability standard involves a trade-off between the price consumers pay for energy and the costs of not having it when needed. Consumers are not often directly involved in these decisions and have limited awareness of the trade-off they are being asked to make; however, they ultimately bear any added costs. Increasing the reliability standard or delinking the RERT will see any additional costs being borne by consumers.

### **Options for procurement trigger and procurement volume**

As highlighted in our submission to the Enhanced RERT consultation we support the reliability standard being the procurement trigger.<sup>12</sup> There is no evidence that there is a need for a new mechanism to trigger the procurement of the RERT.

#### Option 1

In its current form the procurement trigger is ambiguous and provides AEMO with a level of discretion. As the AEMC highlights, at the extreme, the practical impact may be that there is no 'real' procurement trigger specified in the National Electricity Rules (NER).<sup>13</sup> We agree that the NER should more explicitly link the procurement trigger to a breach of the reliability standard. We consider that this will provide clarity to stakeholders as to when AEMO can procure reserves, and certainty to AEMO that resources will be available.

EnergyAustralia is supportive of some additional prescription provided to AEMO allowing them to procure an amount to at most:

- Equal a LRC in the medium term (relevant to long-notice and medium-notice RERT).
- Equal a Lack of Reserve 2 (LOR2) condition in the short term.

#### Option 2

We do not support AEMO's economic assessment framework and it is still not clear to EnergyAustralia what AEMO's proposed solution would look like in its final form. We agree with the AEMC's conclusion that the economic assessment framework is, in essence, the same process that is currently undertaken to determine the reliability standard. Further, AEMO does not have financial incentives to make trade-offs to determine the appropriate level of reserves to procure. They may in fact have reputational incentives, as the system operator, to procure more reserves than may be necessary, with costs borne by consumers. Any form of out of market standing reserve

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<sup>12</sup> EnergyAustralia submission to Enhanced RERT consultation, [https://www.aemc.gov.au/sites/default/files/2018-07/EnergyAustralia\\_1.PDF](https://www.aemc.gov.au/sites/default/files/2018-07/EnergyAustralia_1.PDF)

<sup>13</sup> AEMC Option paper, page 42, <https://www.aemc.gov.au/sites/default/files/2018-10/Options%20paper.pdf>

risks resources being incentivised to leave the market in favour of a 'RERT market'. Not only would this increase costs to consumers but risks also making the reliability of the system worse, hence further increasing reserve costs.

### Option 3

The AEMC's option 3 proposes changes to how AEMO operationalises the reliability standard. Currently the expected USE under the reliability standard is expressed on an annual basis. Option 3 seeks to apportion this annual expected USE across multiple timeframes (for example, monthly, seasonal or quarterly timeframes) which would provide AEMO with an operational RERT trigger directly linked to the reliability standard. The NER or RERT Guidelines<sup>14</sup> may then specify how the gap is forecast (volume to be procured). For example, the difference between a monthly expected USE and the monthly reliability standard. It is likely that the Reliability Panel is best positioned to provide guidance on what finite USE AEMO should target and the most suitable timeframe. We consider this option has potential and welcome more work being completed by the AEMC on it.

### Combining options

A variation on option 3 would be for the NER or RERT Guidelines to provide high level guidance on the volume to procure (at the chosen suitable timeframe), capped at just meeting the reliability standard. AEMO could then use their economic assessment framework (effectively a far more constrained option 2) to determine how much to procure. This would prevent the outcome where AEMO is forced to procure a specific volume (to meet the gap) regardless of reserve cost. A similar approach could also be applied to option 1 with AEMO using their economic assessment framework to determine the volume to procure (capped at meeting the reliability standard).

EnergyAustralia appreciates that AEMO is best positioned to understand the needs of the power system and the operational capabilities of reserve providers. Care needs to be taken to not overprescribe what AEMO should do. However, this is on the provision that there are improvements to the current transparency and reporting<sup>15</sup> requirements of the RERT framework. We consider that AEMO should have some degree of flexibility to make decisions, we should rely on their expertise, and then judge them by results.

Given the above points EnergyAustralia is supportive of option 1 and 3. We consider that there is potential for AEMO's economic assessment (option 2) to be also used in both these options to assist in determining the volume of RERT to procure (capped at meeting the reliability standard). We welcome further work by the AEMC on this, particularly the feasibility of option 3.

## **Conclusion**

While we recognise that at times there will be a requirement for reserves in the NEM, any design of a reserve mechanism should first and foremost encourage generation and demand response to participate in the market. EnergyAustralia does not consider the

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<sup>14</sup> The Reliability Panel is required to produce RERT Guidelines under NER 3.20.8

<sup>15</sup> For example the Australian Energy Regulator (AER) completing a consumer survey and or publishing an independent report on AEMO's RERT process, this was suggested in our submission to the initial consultation, page 5 [https://www.aemc.gov.au/sites/default/files/2018-07/EnergyAustralia\\_1.PDF](https://www.aemc.gov.au/sites/default/files/2018-07/EnergyAustralia_1.PDF)

creation of a standing reserve is in the long-term interest of consumers. We remain concerned about the distortionary impacts this may have on the market. Procuring and activating the RERT should be used only as a last resort intervention by AEMO and at the latest time possible.

The reliability standard remains fit for purpose and should continue to be used as the procurement trigger for RERT. There is no indication that consumers are willing to pay for a higher standard. However, we consider that the NER should be changed to explicitly link the RERT procurement trigger to the reliability standard.

We are supportive of components of both option 1 and 3 and see that the economic assessment proposed by AEMO in option 2 could be used in these to further improve outcomes for consumers. EnergyAustralia looks forward to reviewing further work from the AEMC on this.

If you would like to discuss this submission, please contact Andrew Godfrey on 03 8628 1630 or [Andrew.Godfrey@energyaustralia.com.au](mailto:Andrew.Godfrey@energyaustralia.com.au).

Regards

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