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Australian Energy Market Commission
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Coordination of generation and transmission investment review (CoGaTI) implementation - access and charging Consultation paper

Snowy Hydro Limited welcomes the opportunity to comment on matters raised in the Consultation Paper from the Australian Energy Market Commission (the Commission) on the CoGaTI implementation - access and charging.

Snowy Hydro Limited is a producer, supplier, trader and retailer of energy in the National Electricity Market ('NEM') and a leading provider of risk management financial hedge contracts. We are an integrated energy company with more than 5,500 megawatts (MW) of generating capacity. We are one of Australia's largest renewable generators, the third largest generator by capacity and the fourth largest retailer in the NEM through our award-winning retail energy companies - Red Energy and Lumo Energy.

Snowy Hydro understand that the Commission is required to report biennially on when the transmission planning and investment decision-making frameworks will need to change, given the state of the power system, by the COAG Energy Council. We however strongly oppose the proposed reform by the Commission for dynamic regional pricing and firm access rights. The current NEM approach on the demand side yields more predictable pricing and more simplicity for the retail market while also facilitating competition. Further, the current NEM approach is also significantly easier from a risk management point of view.

Competition can be much better facilitated through increased interconnection between major load centres in the NEM with the current status quo of open access supplemented by more strategic planning of the transmission network. It is for this reason we strongly oppose the costly dynamic regional pricing and firm access rights reform through the phased approach to minimise the level of market disruption and to maximise overall benefits for consumers.

Dynamic regional pricing and firm access will not solve the range of issues noted by the Commission in the consultation paper. Snowy Hydro's concerns are as follows:

- There is no evidence that greater accuracy will assist those parties affected by adverse marginal loss factors (MLF).
- Disorderly bidding has already been addressed in numerous current rule changes. The rule change on Bidding in Good Faith was implemented to stop the conduct of concern and to make it easier for the AER to take enforcement action in respect of deliberately late rebidding. In addition, the Commission has not properly assessed the implementation of 5 minute settlement before proposing another significantly costly reform.
- Access reform will not encourage investment where it is needed. Factors such as availability of resources (fuel and land) and political guidelines for renewable energy and availability of

fuel often place new generation away from demand centers. These factors will only override the locational signals from the nodal price.

This is not the time for the Commission to make a significant change to transmission access arrangements when there is uncertainty in the current environment. The current process to relieve transmission network congestion is adequate at ensuring transmission investment is developed in conjunction with generation developments.

The implementation dates proposed for access reform are unreasonably ambitious. If there is a need to review elements of the access reform then Snowy Hydro believes the ESB Post 2025 Market Design work, which is assessing different market designs, would also require a new access regime to be looked at. The clear solution from this dilemma is that work on access in the status-quo design should be merged into the post-2025 market design review.

If there is to be further work however by the Commission then Snowy Hydro strongly support a proper cost benefit analysis on the impact of dynamic regional pricing and firm access arrangements being undertaken. This would properly consider the operational costly impacts the reforms will have on market participants and the risks for consumers.

Congestion

Australia has a liquid financial market that offers a range of forward contracts. In addition there are liquid markets for various products in bilateral trade, such as contracts for differences between zones. There are no transmission rights, neither physical nor financial in the Australian market. In addition the NEM has not experienced significant congestion and any imbalances have been managed through the dispatch process.

The Consultation Paper notes that it is *“not sustainable for either generators or customers given increasing levels of congestion”*. Snowy Hydro are concerned by the Commission's note and their proposal. It was only last year the Commission engaged Ernst & Young (EY) to assess patterns and costs of congestion in the NEM. *“The EY work demonstrated that there are limited amounts of congestion in the NEM at the moment – and of that which does occur, it is largely between regions (that is “inter-regionally”). There is limited congestion within regions to date.”*¹

With the significant growth in proposed new generation it is important that investors have sufficient confidence in the market and the overall policy settings to deliver the capital prevent any future significant congestion issues. Market participants will not gain confidence from a significant and costly access reform.

The challenge for long-term efficiency in transmission lines stems from the fact that transmission assets take a long time to site and build, are very long-lived and economically disruptive investments. This means that the AER's large scale review of the application guidelines for the regulatory investment tests (RITs) and AEMO's ISP takes on greater importance on the future impact of congestion.

Need for access reform

The Commission should undertake a comprehensive understanding of the interactions between the current rule changes before proposing significant and costly changes to the market. Snowy Hydro is

¹ AEMC 2018, Coordination of generation and transmission investment, Discussion paper, 13 April 2018, Sydney

unclear by the Consultation Paper's assessment on the range of issues currently being experienced between transmission and generation and being solved or improved by access reform.

The Commission notes that there are several types of disorderly bidding behaviours that can occur in the NEM. Snowy Hydro however is concerned on the timing and reasoning for proposing such a costly reform to improve disorderly bidding when the key benefit was that the 5 minute settlement proposal would improve price signals for more efficient generation and use of electricity, improved price signals for more efficient investment in capacity and improved bidding incentives². The Commission should properly assess the benefits from 5 minute settlement once implemented before imposing a costly reform on the market.

Further to this the Commission notes in the supplementary paper that five minute settlement will not solve a particular type of disorderly bidding which exposes generators to the dynamic regional price and removes the incentives to disorderly bid when transmission constraints arise. This issue has not been noted previously in COGATI reports by the Commission as a significant problem and the Bidding in Good Faith rule change has not been mentioned³. The rule change was implemented to stop the conduct of concern and to make it easier for the AER to take enforcement action in respect of deliberately late rebidding. We are concerned that the Commission could be left making significant rule changes which the Bidding in Good Faith⁴ rule was implemented to prevent. Bidding in Good Faith was put in place so as to lead to more efficient wholesale price outcomes in the short term, and create investment signals that better reflect underlying conditions of supply and demand, in the long term interests of consumers.

The reform on dynamic pricing is a complex solution looking for a problem. Reforms should not be implemented or proposed without understanding the implications it could have on the NEM and on consumers.

The Commission notes that one of the issues dynamic nodal pricing could improve is marginal loss factors (MLF). The consultation paper notes that *"given the large number of generators connecting at the moment, and the fact that marginal loss factors inherently change after a new generator connects to the network, this is resulting in significant year-on-year fluctuations in the marginal loss factors."*⁵ Snowy Hydro however note that losses in a transmission network are a natural physical phenomenon.

It is unclear if greater accuracy will assist those parties affected by adverse MLFs, as there is no reason to expect that greater accuracy would significantly improve the market participants circumstances. The regional market design, combined with static yearly loss factors is the result of an initial simplification decision that, as a trade-off, introduced some inaccuracy⁶. It would be more appropriate to re-assess whether, given the changes in the power system, the trade-off continues to represent the correct balance rather than proposing a significant change to the NEM which would not entirely solve the problem it set out to solve.

The Commission notes in the supplementary paper that firm transmission rights would *"create a clear and cost-reflective locational signal for new generation investment that is currently missing in the NEM."*⁷ Snowy Hydro strongly believes that this will not encourage investment where it is

² AEMC, Five Minute Settlement, final determination, 28 November 2017, Sydney

³ AEMC, 2017, "National Electricity Amendment (Bidding in Good Faith) Rule 2015"

⁴ AEMC, 2017, "National Electricity Amendment (Bidding in Good Faith) Rule 2015"

⁵ AEMC, CoGaTI implementation - access and charging, Consultation paper, 1 March 2019, pp10

⁶ Australian Energy Council, 2019, "Marginal Loss Factors: Will someone please repeal the laws of physics?"

⁷ AEMC, CoGaTi implementation - access and charging, Supplementary information paper, 4 April 2019, pp7

needed. Factors such as availability of resources (fuel and land) and political guidelines for renewable energy and availability of fuel often place new generation away from demand centers. These factors will only override the locational signals from the nodal price. It is therefore difficult to prove that a nodal system or firm access actually leads to more “correctly” located investments in generation and network than the current system, and implies the concept of “correctly” located investments is somewhat more complex and subtle than a simple reading of the nodal price signal would suggest.

Nodal pricing markets such as the PJM have additional support mechanisms to encourage investments, implying that at least these implementations of nodal pricing have not historically provided sufficient investment signals.

What is the likely impact on contract liquidity of the access reform?

Snowy Hydro considers that under the current market arrangements there is a well-defined method of allocating transmission capacity. There is no basis risk as the generator receives the regional reference price when it is dispatched. In contrast, under firm access, Snowy Hydro considers that volume risk would still exist as dispatch would not be guaranteed. Additionally there would be basis risk if a proportion of a generator's output is priced at its local price. In Snowy Hydro's view, this additional basis risk would adversely impact the functionality and liquidity of the contract markets. This additional risk would not lead to lower electricity bills for consumers.

Cost benefit analysis

The supplementary information paper⁸ notes that the last transmission review undertaken in 2015 by the Commission on Optional Firm Access (OFA) would not contribute to the achievement of the National Electricity Objective following an assessment of the benefits and the costs. Further to this, in 2015, Frontier, on behalf of a group of NEM participants (AGL Energy, Origin Energy, Snowy Hydro and Hydro Tasmania), found that OFA does not offer an appropriate way forward for the NEM, irrespective of potential future changes in market conditions and uncertainty regarding generation technologies and costs. The Frontier report also noted that the Commission did not establish the existence of significant problems in the current market design that OFA would be likely to address. OFA could increase rather than reduce the risks faced by consumers and would be more likely to harm the efficiency of generation and transmission investment coordination than to improve it⁹. Following the significant similarities to the issues noted in 2015, Snowy Hydro oppose the Commission's phased access reforms which would require firm access.

Finally in 2015 the Commission found that the benefits of OFA did not outweigh the costs with the OFA not offering an appropriate way forward for the NEM, irrespective of potential future changes in market conditions and uncertainty regarding generation technologies and costs. The Commission at the time did not establish the existence of significant problems in the current market design that OFA would be likely to address. Two years later the same arguments apply.¹⁰

Snowy Hydro strongly believes undertaking a proper cost benefit analysis on the impact of dynamic nodal pricing and firm access arrangements before there is a further assessment on the proposed reforms. It is important that the Commission doesn't fail to consider the operational costly impacts

⁸ AEMC, CoGaTi implementation - access and charging, Supplementary information paper, 4 April 2019, pp7

⁹ Frontier Report On Optional Firm Access, <<
<https://www.frontier-economics.com.au/frontier-report-optional-firm-access-published-aemc/> >>

¹⁰ Frontier, 2015, “Response to OFA Draft Report”, pg iii

the reforms will have on market participants and the risks for consumers in terms of cost, reliability and system security.

Timing

Market Participants are currently responding to potential wide-ranging reforms to the security and reliability frameworks in the NEM. Snowy Hydro asserts this is not the time for the Commission to make a significant change to transmission access arrangements when there is uncertainty in the current environment. The reform is clearly a problem looking for a solution and will unfairly discriminate against large-scale generation by requiring them to pay to access the transmission network and overcomplicate the NEM through dynamic regional pricing. It would increase rather than reduce the risks faced by consumers and would be more likely to harm the efficiency of generation and transmission investment coordination than to improve it.

Snowy Hydro believes the ESB Post 2025 Market Design work, which is assessing different market designs, would also require a new access regime to be looked at. The clear solution from this dilemma is that work on access in the status-quo design should be merged into the post-2025 market design review.

Snowy Hydro appreciates the opportunity to respond to the Consultation Paper and any questions about this submission should be addressed to Panos Priftakis, Regulation Manager, by e-mail to panos.priftakis@snowyhydro.com.au.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'K Ly', with a horizontal line underneath.

Kevin Ly
Head of Wholesale Regulation
Snowy Hydro