Government of South Australia

D19117842

27 November 2019

Mr John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Dear Mr ~~Pierce~~, John

RE: EPR0073 – COORDINATION OF GENERATION AND TRANSMISSION INVESTMENT IMPLEMENTATION – ACCESS AND CHARGING

The Energy and Technical Regulation Division ('Division') of the Department for Energy and Mining thank you for the opportunity to make a submission on the *Coordination of generation and transmission investment implementation – access and charging* review (*EPR0073*).

As stated in our response to the AEMC's direction paper that was released on 27 June 2019, the Division considers that access and congestion management issues need to be addressed with urgency. Reforms implemented as part of the Coordination of generation and transmission investment (COGATI) review will continue to support the development and delivery of affordable, reliable and secure energy supplies in a transitioning national energy market. We therefore commend the AEMC's commitment to the final report being delivered in December 2019 and to the broader timeframes for implementing the new access regime in July 2022 through a rule change process commencing in early 2020.

Recognising that the AEMC published two Discussion Papers for consultation, the *Coordination of generation and transmission infrastructure proposed access model Discussion Paper and the Renewable Energy Zones Discussion Paper*, our response is set out to provide information on each Discussion Paper.

<u>COGATI Proposed Access Model</u>

The Division agrees that scheduled and semi-scheduled market participants should be exposed to a local price ('locational marginal price' (LMP)), as this more accurately represents the marginal cost of supplying electricity at their location in the network and considers factors such as constraints on the transmission network and the marginal losses at the transmission connection point.

The Division considers that the introduction of dynamic regional pricing should reduce and/or eliminate the 'race to the floor' bidding by generators when the system is congested and would expect that the AEMC undertakes further analysis on the benefits of removing this behaviour as part of its planned quantitative analysis.

In addition, the Division also supports the adoption of dynamic loss factors – recognising that more efficient dispatch of generation will be achieved. The Division was recently advised by generation representatives that whilst adopting dynamic losses would reflect the efficient dispatch of generation, there is no hedging mechanism currently available to manage the existing volatility that is being experienced through marginal loss factors (MLFs). The introduction of Financial Transmission Rights (FTRs) should therefore address this for current and future generation.

It is well recognised that there is limited liquidity in the contracts market in South Australia. The Division therefore supports the AEMC's consideration of contract market liquidity when developing its dynamic pricing model, with non-scheduled market participants continuing to be settled at a common regional price for wholesale electricity.

The Division supports the AEMC's proposal to establish FTRs to help market participants manage the increasing volatility and unpredictability of congestion and losses that arise as a result of the transitioning power system.

The Division agrees that the proposed design of FTRs is likely to improve the liquidity of contract markets as they would allow scheduled and semi-scheduled market participants to manage transmission congestion risk more effectively than they can under the current arrangements.

The Division also agrees that FTRs between regions should replace the settlement residue auction (SRA) as they would provide a firmer hedge than the existing SRA units. As noted by the AEMC, this should improve the ability for market participants to manage pricing risk across regions, improve regional trade and improve liquidity in the existing regional markets. Improved regional trade will be extremely important in utilising the diversity of renewable generation assets as the market transitions towards a lower emissions future.

The Division agrees that the proceeds from FTR auctions should be returned to customers via reduced transmission use of service (TUOS) charges. However, further information is required on how the auction process will take place, and the transparency measures that will be implemented by the AEMC in order to ensure that the full amount of the FTR auctions are returned to customers through reduced TUOS charges.

<u>Renewable Energy Zones</u>

Whilst the Division recognises the issues the AEMC's proposed model attempts to address, including the free-rider problem encountered today, the Division is mindful that this proposed model potentially introduces new risks for consumers.

As noted by the AEMC – if generator interest covered less than 100% of the cost, the residual cost would either need to be taken on as a risk by the Transmission Network Service Providers (TNSPs) or paid for by consumers as a prescribed transmission service.

Historically, TNSPs have not demonstrated an interest in assuming the risk of transmission network outside of economic regulatory framework investment or customer funded investment. Existing evidence suggests that TNSPs are more likely to seek to recover the residual cost from consumers. Therefore, the AEMC is encouraged to focus on this scenario when considering whether the proposed model is in the long-term interests of consumers.

The Division considers that where the Regulatory Investment test for transmission (RIT-T) has determined investment in a REZ is in the best interest of consumers, any uncommitted capacity should be available through the FTR auction process, with proceeds returning to consumers through reductions in TUOS charges, under the AEMC's proposed access model. This would maintain the appropriate incentives for generators to invest in a REZ as doing so would provide them access to long-term transmission hedges and avoid having to compete against other market participants, and potentially missing out, through the FTR auction process.

Thank you for accepting our submission. Should you wish to discuss this further, please contact Mr Mark Pedler, Principal Policy Officer, on (08) 8429 3361.

Yours sincerely,

Vince Duffy
Executive Director, Energy and Technical Regulation