

SCOPE

This submission covers the following:

- ERC0290: Hydro Tasmania — *Synchronous service markets*
- ERC0300: TransGrid — *Efficient management of system strength on the power system*
- ERC0296: Infigen Energy — *Fast frequency response market ancillary service*
- ERC0295: Infigen Energy — *Operating reserve market*
- ERC0306: Delta Electricity — *Capacity commitment mechanism for system security and reliability services*
- ERC0307: Delta Electricity — *Ramping services*

INTRODUCTION

The Energy Users Association of Australia (EUAA) is the peak body representing Australian commercial and industrial energy users. Our membership covers a broad cross section of the Australian economy including significant retail, manufacturing, food and materials processing industries. Combined our members employ over 1 million Australians, pay billions in energy bills every year and expect to see all parts of the energy supply chain making their contribution to the National Electricity Objective.

Our members are highly exposed to movements in both gas and electricity prices and have been under increasing stress due to escalating energy costs. These increased costs are either absorbed by the business, making it more difficult to maintain existing levels of employment or passed through to consumers in the form of increases in the prices paid for many everyday items.

We welcome the opportunity to respond to the System Services Rule Changes Consultation Paper (Consultation Paper) and appreciate the work being carried out by the AEMC and ESB to synthesise the many parallel policy and regulatory processes currently underway.

It is clear that the rule change requests discussed in the Consultation Paper cross paths with a number of other work streams being pursued by AEMO, ESB and AEMC. We trust that all market bodies and government can achieve a high level of coordination to avoid duplication of effort and most importantly, avoid the creation of new markets and/or mechanisms that increase costs for consumers.

Our understanding of these concurrent processes is that an overarching post 2025 market framework is being developed that will ensure the NEM is fit for purpose for the decades ahead. This process should include the identification of potential gaps that may need to be filled by new policy, regulation or market rules. We look forward to contributing to the development of this new architecture with the forthcoming publication of the post 2025 Consultation Paper.

This leads us to the firm view that the rule change requests described in the Consultation Paper are somewhat premature and would be best assessed as part of the broader post 2025 work program, including the identification of gaps in policy, regulation and market rules.

In any event, we do not believe the proponents have provided sufficient justification to pursue these rule changes at this point in time, or at all. In the absence of a clear articulation of where they may fit into the post 2025 market design framework and without robust cost benefit analysis to support their assertions of consumer benefits, it is virtually impossible for us to provide our support to pursuing any of the proposed rule changes.

If at the completion of the broader post 2025 work program any of these rule changes are deemed necessary we expect that a more complete package of reforms is presented to consumers that includes independently verified cost benefit analysis and a framework for more appropriate cost and risk allocation.

ENERGY MARKET TRANSFORMATION

The EUAA fully appreciates the magnitude of the transformation that our energy markets are experiencing and the potential impacts on cost, risk, reliability, security and environmental sustainability. This transformation is no more profound than in energy generation where, over the last 15 years we have moved from a government owned, highly centralised, thermal generation fleet to a predominantly privately owned, highly dispersed generation fleet that is progressively dominated by variable renewable energy resources.

There are many positives associated with renewable energy and the transition to a low emissions energy market is well underway. However, non-synchronous generation can't replicate the system strength characteristics of the synchronous generation it is replacing. Therefore, the large scale integration of non-synchronous generation is posing new and significant challenges for energy markets including those associated with maintaining system strength.

Therefore, progressively moving away from synchronous generation will drive the need to replicate the system strength characteristics it naturally provides. This may require the need for existing technology to operate differently or for new technologies to be deployed in conjunction with non-synchronous generation to ensure system strength is maintained. In some, but not all cases, this may require new incentives to be created via markets or additional requirements on generators through regulation.

When it comes to energy supply, energy users are technology neutral and simply require a product that is provided at least cost, that is safe, that is reliable, that is fit for purpose and progressively that it is environmentally sustainable. Therefore, we are more concerned with the means by which technology is deployed rather than what technology is being deployed, always ensuring that the approach taken leads to the least cost outcome for consumers.

Therefore, when looking at any rule change request, policy option or regulatory design, the key questions for energy users are:

- Has a genuine need been established or gap identified that can't be resolved within existing market and commercial arrangements (or with modest adjustments to existing arrangements)?
- Where does this fit into the overarching policy and regulatory approach?
- Once a clear need has been established, what is the optimal approach to bring about the desired outcome such that it delivers the least cost outcome for consumers recognising that both markets and regulation can deliver this outcome?
- Has a robust cost benefit analysis been conducted that demonstrates irrefutable positive outcomes for consumers?

- Are the costs and risks appropriately apportioned?

This final point has been a key area of EUAA advocacy in recent years. It is our strong desire to ensure that all market participants face the costs and risks they are either directly responsible for or are in the best position to manage. Equally, we believe that the more of these costs and risks that are directly exposed to competitive forces, the more likely it is that consumers will benefit from a least cost outcome.

Given this, we tend to favour policy and regulatory responses that are guided by the “causer pays” approach. This is why we support continuation of the “do no harm” concept as a prominent guiding principle to ensure fair and reasonable outcomes are achieved for all market participants.

Facing these costs and risks directly would incentivise appropriate investment and operational decisions by market participants with the cost of compliance either being absorbed into the overall cost base of the market participant or passed through to consumers (either in part or in full) depending on their competitive position.

Therefore, in assessing any rule change, including those proposed in this Consultation Paper, we urge the AEMC to give consideration to the most appropriate method of incentivising market participant behaviour recognising that simply creating another market may not always lead to the least cost outcome for consumers and may in fact deliver windfall gains to some market participants.

RESPONSES TO SPECIFIC QUESTIONS

The issues raised in the Consultation Paper are substantive in number and complexity. Many of the questions relate directly to the daily activities of market participants and while the outcomes may have impacts on consumers by way of cost, reliability and system strength, consumers do not have the direct operational knowledge that market participants (or market bodies) have in these areas.

In any case, as we have stated earlier in this submission, we do not believe the proponents have provided sufficient justification to pursue these rule changes at this point in time, or at all. In addition to this, it is not clear where these rule changes fit into the post 2025 market design while the absence of robust cost benefit analysis to support their assertions of consumer benefits is also concerning.

As a consequence of this, it is virtually impossible for us to make a value judgement on or provide our support to any of the proposed rule changes at this point in time. Therefore, we will not attempt to provide answers to all of the 103 questions asked in the Consultation Paper but will provide broad, more principles-based comments where we believe we can add value to the overall process.

If at the completion of the broader post 2025 work program any of these rule changes are deemed necessary we expect that a more complete package of reforms is presented to consumers that includes independently verified cost benefit analysis and a framework for more appropriate cost and risk allocation. An appropriate vehicle for this could be a well targeted Directions Paper.

This being the case, we would be better equipped to make a more detailed and informed submission on individual rules.

QUESTION 1: CURRENT ESB & AEMO WORK RELATING TO THE RULE CHANGE REQUESTS

1. What are stakeholders' views on how the rule change processes should be integrated with ESB and AEMO work programs?

On page 4 of the Consultation Paper the following statement is made:

“The rule change requests complement and are interdependent with the work of the ESB in its 2025 project. These rule changes provide us with an opportunity to complement some of the thinking and assessment done in the ESB work program, as well as technical input from AEMO through its Renewable integration study. It allows us to address the issues in a cohesive way, as well as addressing system security issues that are more urgent in nature.”

While we are not in a position to make comment on the complimentary nature of these rule change requests with the broader post 2025 work program we do agree that the rule change requests overlap many of the issues already being considered by both the ESB and AEMO. In time, some of the proposed rule changes may demonstrate clear net benefits as part of a broader post 2025 market design so we strongly recommend they be incorporated into these broader market reform processes.

In addition to this, the Consultation Paper identifies two important and highly relevant concurrent processes being:

- The AEMC's *Investigation into system strength frameworks in the NEM*
- The AEMC's assessment of AEMO's rule change request, *Primary frequency response incentive arrangements*.

It seems logical to view the rule change requests outlined in the Consultation Paper in light of these concurrent AEMC processes, which may identify the need (or lack thereof) for individual rule changes.

We encourage both the ESB and AEMO to work closely with the AEMC and industry stakeholders to use this rule change process, of which we are at the very start, to properly assess the need, scope, cost and benefits of the proposed rule changes and to bring forward a consolidated group of reforms as part of the broader post 2025 market design and renewable integration projects.

2. Are there any additional processes that should be closely considered by the Commission when progressing these rule change requests?

One of the key outcomes of the proposed rule changes will be the deployment of physical assets to support system strength and reliability. There are a number of state and federal initiatives either already in place or well advanced that seek to achieve similar outcomes. These include the Federal Government UNGI program and support for Snowy 2.0, both of which will drive investment in new flexible generation that would achieve reliability and system strength outcomes.

While there may be a role for governments to shield consumers from risk and costs, to be reliant on government subsidy programs as the sole driver for both system strength and reliability is not ideal. We are not opining on the validity of these government actions but take this opportunity to point out it is happening and we need to be conscious of both positive and negative consequences of such actions.

We would also point to the AEMO 2020 ISP which asserts that a more integrated system will facilitate the sharing of system services across regions, an assumption that may be contradicted by some of the potential outcomes of the proposed rule changes that may lead to the deployment of new resources within regions (assuming system strength continues to be assessed on a regional basis).

If so, we need to remain conscious of the cost and benefits of facilitating shared NEM wide services vs localised system service provision and ensure that we guard against the “gold plating” of system strength. In this regard we urge AEMO to remain vigilant as to the deployment of technologies within regions so as to avoid unnecessary network investment.

The absence of a market to deploy assets that assist with system strength has not seemed to hamper actual investments in this area.

For example, AGL have recently commissioned the 210MW Barker Inlet gas fired power station in South Australia and have announced plans to replace Liddell power station with up to 500MW in battery capacity¹. Origin Energy have also announced a 100MW expansion of their Mortlake gas fired power station² while large scale batteries are already in operation in South Australia with more planned.

While not expressly motivated by solely providing system strength services these physical assets do deliver system benefits such as frequency, inertia and ramping services. Importantly, many of these assets are being committed, in growing numbers in the case of large-scale batteries, despite the absence of the markets being contemplated by the proposed rule changes.

Therefore, the proposed rule changes should be carefully considered so as to avoid rewarding market participants for services they are already providing (or seeking to provide) or that could be provided under existing market or contract arrangements.

For example, deployment of technologies to deliver some of these system services are likely to be influenced by the WDRM, RRO or the revised Reliability Standard of .0006 while existing hedging arrangements could be adapted to manage other issues identified by rule change proponents.

We would encourage the AEMC to look very closely at what existing arrangements are likely to deliver the required system strength outcomes before jumping into the creation of a new market (and consumer cost) that may not be needed. To do so could deliver windfall gains to some market participants without necessarily improving system strength outcomes beyond what would evolve naturally.

Rule changes should focus on delivering system services where there is a genuine gap that is not already being filled or capable of being filled under existing arrangements or modest modifications to them or through the enforcement of well-considered “do no harm” regulations.

QUESTION 2: TIMETABLE FOR THE CONSULTATION PROCESS

1. Do stakeholders have any comments on the proposed timetable for the system services rule changes?

¹ <https://www.afr.com/companies/energy/agl-s-liddell-plan-out-of-coal-into-batteries/>

² <https://www.standard.net.au/story/6850535/south-west-gas-power-plant-plans-250m-expansion/>

The issues being considered in the Consultation Paper are complex in their own right and more so when taken together with a significant number of concurrent processes. We appreciate AEMC recognising in the Consultation Paper (page 10) the enormous workload on market participants brought about by the unprecedented scope and complexity of the reform process.

“The Commission is also mindful of the challenge for stakeholders keeping track of the large volume of regulatory reforms under way. The coordinated approach to consultation on the system services rule change requests is intended to help reduce this overall burden on stakeholders.”

This is very much the case for consumer groups who simply don’t have the time, resources or deep operational knowledge to perform an analytical deep dive into every rule change, regulatory reform or policy. We would not want to see important and potentially costly rule changes rushed unnecessarily, especially given the risk of overlapping reforms (and cost) of concurrent work being undertaken.

We are in general agreement with the timetable in the Consultation Paper but ask that the AEMC remain conscious that the current regulatory workload combined with the difficulties many stakeholders are facing associated with the COVID pandemic restrictions, may mean that stakeholders require more time to consider these issues than would otherwise have been the case. In any event, synchronising these rule change proposals into the overarching ESB and AEMO work programs would make sense.

QUESTION 3: THREE WORK STREAMS: DISPATCH, COMMITMENT AND INVESTMENT

1. Do stakeholders agree with the AEMC’s approach to grouping the rule changes, at least for initial consideration?

These groupings make sense and allow stakeholders to consider similar issues, costs, benefits and potential for duplication.

2. Do stakeholders believe that Figure 3.1 captures the key issues to be considered for each rule change in each time frame?

While some of the issues are interchangeable across that various groupings in Figure 3.1, we believe it captures the key issues for each of the rule change requests. We would highlight that these groupings seem to assume that the ultimate result will be the creation of new markets for the services identified (assuming an unserved need is identified and in creating a new service that the benefits outweigh costs).

As we have stated previously, we urge the AEMC to consider all approaches to incentivising needed services including a regulatory requirement under “causer pays” and “do no harm” principles.

3. Do stakeholders have views on whether/which services should be procured in certain time frames and not others?

We have no view at this stage other than to say that the overarching market design work being undertaken by the ESB and AEMO should be the primary driver for the creation and timing of new incentives for system services, provided an unserved need has been identified.

QUESTION 4: THE SYSTEM SERVICES OBJECTIVE

1. Do stakeholders agree with the AEMC's proposed system services objective being used to assess these rule changes? If not, how should it be amended or revised?

We agree that the NEO must continue to be the map that the reform agenda must follow. However, there are times when consumers have felt that certain outcomes have not promoted the long-term interests of consumers and that we have not balanced price, quality, safety, reliability and security of supply.

For example, the recent creation of an interim reliability standard that appears to place reliability well above price (or cost) and is viewed by my many consumers as not following the NEO map. This and other measures are being justified to manage what has been described as "tail risk", specifically when multiple unexpected events occur. However, this is likely to represent High Impact Low Probability (HILP) events that consumers have repeatedly stated that, despite their negative impacts, they believe to too expensive to avoid. In other words, it would normally fail a cost benefit assessment.

Similarly, we are yet to be convinced that all (or any) of the rule change requests equally balance these competing objectives of the NEO.

We are not opposed to the creation of a more defined system service objective, which is set out on page 23 of the Consultation Paper, but believe it falls short on achieving a least cost objective for consumers.

*The **system services objective** seeks to:*

Establish arrangements to optimise the reliable, secure and safe provision of energy in the NEM, such that is it provided at efficient cost to consumers over the long-term, where 'efficient cost' implies the arrangements must promote:

- *efficient short-run operation of,*
- *efficient short-run use of, and*
- *efficient longer-term investment in,*

generation facilities, load, storage, networks (i.e. the power system) and other system service capability.

Unfortunately, consumers have found from time to time that what is deemed as "efficient" depends on the perspective of the stakeholder.

For example, we would argue that "efficient cost" doesn't necessarily lead to "least cost" outcomes for consumers. We are certain that if consumers were asked, they would prefer to see a more definitive "least cost" objective being pursued while maintaining current levels of reliability and system strength.

For example. A Network Service Provider (NSP) would rightfully see it as efficient to collaborate with generators to develop a joint technical solution to system strength rather than individual generators developing their own solution independently. On this we would agree. The NSP may also see it as efficient to include the cost of providing this joint technical solution in their Regulated Asset Base. On this we would disagree as we do not think it necessarily leads to a least cost outcome for consumers.

If the cost is included in the NSP RAB then consumers take on the entire cost and risk while the generator takes on none. This essentially displaces the incentive, cost and risk away from those who are best able to manage it (generator and NSP) to those who have absolutely no control (the consumer).

In this situation we would prefer that either of the following approaches:

- Generators continue to provide their own solution, incorporating it into their overall cost base and recovering it via the wholesale energy price or off-take agreement. While it could be argued that this may result in an over-investment by the generators it exposes the costs to a competitive market, increasing the likelihood of lower cost to consumers while ensuring more of the asset related risk rests with the party in the best place to manage it.
- The NSP develops a joint technical solution in collaboration with generators as a non-regulated asset. Generators would then either be co-investors or purchase access rights or usage rights to services provided by it.

In any case, we do not agree with dismantling do no harm provisions as we see it as an important signal to generators of what is expected of them as they connect to the network.

QUESTION 5: THE PLANNING, PROCURING, PRICING AND PAYMENT SERVICE DESIGN FRAMEWORK

1. Do stakeholders agree with the '4Ps' service design framework being used to design these rule changes?

The '4Ps' service design framework appears to be a good starting point for assessment however it seems to assume that all the system services being contemplated are needed and that the creation of new markets is a foregone conclusion. As we have stated before, we don't necessarily think this should be the case.

As we have stated elsewhere in this submission, we do not believe the proponents have provided sufficient justification to pursue these rule changes at this point in time, or at all.

Therefore, we would propose that in addition to the Plan, Procure, Price, Pay elements that a 5th "P" is included at the start of the service design framework. The first "P" being Problem, the definition of which is "Has a genuine problem been identified that can't be managed within the current market frameworks? If so, are these problems being addressed in a concurrent process? And finally, Will the resolution of this problem deliver a least cost outcome for consumers?"

Therefore, we think the design framework should be Problem, Plan, Procure, Price, Pay.

QUESTION 6: PRINCIPLES FOR ASSESSMENT

1. Do stakeholders agree the principles proposed for assessing the rule change requests are appropriate? If not, which should be amended, excluded or added?

The principles for assessment being:

- Promoting power system security and reliability
- Appropriate risk allocation
- Technology neutral

- Flexibility
- Transparent, predictable and simple

seem reasonable with the inclusion of appropriate risk allocation a welcome addition. However, we would like to see a more definitive assessment of costs and benefits included as key principles for assessment

We find objectives such as below (page 26) to be less than compelling for consumers who are focused on the cost of energy as a key input to their business and would like to see cost as a central principle rather than simply having regard for it:

“It is therefore necessary to have regard to the potential benefits associated with improvements to system security and reliability brought about by the proposed rule changes, weighed against the likely costs.”

Our concerns are heightened on this issue given recent history of not balancing costs and risks. With the “gold plating” of networks in the past consumers have already experienced a negative outcome of a reform processes that appeared to have just “given regard” to costs, relegating this key consumer indicator to a secondary objective until it was too late.

We trust that all of our market bodies (and market participants) have consumer costs at the forefront of their thinking as we move through these unprecedented times and would therefore encourage the AEMC to place consumer cost at the head of the queue when developing principles for assessment.

For example, we consider the following re-wording of the above statement would better reflect this:

*“It is therefore necessary **for rule change proponents** to have regard to **ensure** the potential **likely** benefits associated with improvements to system security and reliability brought about by the proposed rule changes **can be clearly identified, are independently verified and far outweigh** weighed against the likely **range of** costs.”*

QUESTION 13: EVOLVING THE REGULATORY DEFINITION OF SYSTEM STRENGTH & QUESTION 14: MECHANISMS FOR SYSTEM STRENGTH ABOVE MINIMUM LEVELS NECESSARY FOR SYSTEM SECURITY

It is the expectation of the EUAA and its member companies that the central product of the energy industry, being the supply of electrons, is provided at least cost, is provided safely, is provided reliably, is provided in a way that is fit for purpose and progressively that it is environmentally sustainable. This is no different to consumer expectations of the provision of any other service such as gas, water, public transport, mail services etc.

How this service is provided to the satisfaction of the consumer is the responsibility of both governing bodies and market participants. Therefore, as consumers, we do not have a view on how the service is delivered, just on the price, quality and safety of it.

QUESTION 15: REQUIREMENT FOR AN EXPLICIT IN-MARKET RESERVE MECHANISM OR MARKET IN THE NEM & QUESTION 16: ACHIEVING SECURITY OR RELIABILITY OUTCOMES USING A NEW IN-MARKET RESERVE MARKET OR MECHANISM?

The discussion of creating an explicit in market reserve is somewhat premature and largely ignores the fact that we already have both the Retailer Reliability Obligation (RRO) and Wholesale Demand Response Mechanism (WDRM) that are designed to have the effect of creating a form of in-market reserve.

We are also led to believe that, with these mechanisms functioning correctly the RERT will not need to be activated to the levels we have seen in recent years.

Therefore, we do not support the creation of an explicit in market reserve until such time that we have concluded the current framework, including RRO and WDRM is failing to achieve what was intended.

QUESTION 17: REFORMS RELATED TO THE PROVISION OF SYNCHRONOUS INERTIA

While declining system inertia will continue to be an issue, we urge the AEMC to consider a range of approaches to dealing with this problem including strengthening do no harm provisions of connecting generators and enhancing the scale efficient network extension framework to include technologies associated with system strength.

We must seek to ensure the investive is targeted at the right link in the value chain to ensure change of behaviour and appropriate investment occurs at the point of origin (i.e. generator level) rather than at a point somewhat removed from the problem we seek to resolve.

QUESTION 22: COST RECOVERY ARRANGEMENTS

The Consultation Paper provides a summary of potential cost recovery arrangements on page 79:

There are a range of different ways that costs are allocated and recovered in the NEM. For example:

- **Causer pays** — where costs are recovered from the parties that caused the need for a service to be procured. For example, the costs of procuring regulation FCAS are recovered from market participants who have been found to have contributed to the need for frequency regulation in the recent past.
- **User pays** — where the person or participant using the service or asset pays for it. This is a common form of cost recovery in the NEM. For example, it is used by networks when recovering the costs of an asset that is built for the sole use and benefit of one party.
- **Beneficiary pays** - similar to user pays, this model generally seeks to require those users that are seen to ‘benefit’ from the use of a service or asset, pay for it. For example, the arrangements for the recovery of system restart ancillary services costs can be considered, at least in part, to reflect this principle, as both generators and customers benefit from the service, and therefore pay equal shares for its provision.
- **Smearred recovery from a broad group of customers** — for example the recovery of RERT costs are smearred across those market customers that were consuming energy at the time of RERT activation based on their share of energy consumption.
- **Market participant fees** — where costs are recovered at regular intervals from registered market participants. For example, AEMO's operating costs are recovered in this way.

As we have stated elsewhere in this submission, we are strongly drawn to the principles of causer and user pays approaches. It is our strong desire to ensure that all market participants face the costs and risks they are either directly responsible for or, are in the best position to manage. This is consistent with our view supporting continuation of the application of the “do no harm” principle to ensure fair and reasonable outcomes are achieved for all market participants.

QUESTION 23: IMPLEMENTATION CONSIDERATIONS

It is clear that the rule change requests discussed in the Consultation Paper cross paths with a number of other work streams being pursued by AEMO, ESB and AEMC. These concurrent processes will create an overarching post 2025 market framework that will ensure the NEM is fit for purpose for the decades ahead. This process should include the identification of potential gaps that may need to be filled by new policy, regulation or market rules. We understand much of this new architecture will be revealed toward the end of 2020.

This leads us to the firm view that the rule change requests described in the Consultation Paper are somewhat premature and would be best assessed as part of the broader post 2025 work program, including the identification of gaps in policy, regulation and market rules.

In any event, we do not believe the proponents have provided sufficient justification to pursue these rule changes at this point in time, or at all. In the absence of a clear articulation of where they may fit into the post 2025 market design framework and without robust cost benefit analysis to support their assertions of consumer benefits, it is virtually impossible for us to provide our support to pursuing any of the proposed rule changes.

Sincerely,



Andrew Richards
Chief Executive Officer