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Mr Ben Hiron
Project Leader
Australian Energy Market Commission

Submitted via the AEMC Website

ERC0263 – Primary Frequency Response Incentive Arrangements – Draft Determination

Alinta Energy welcomes the opportunity to respond to the Commission's draft determination on the Primary Frequency Response Incentive Arrangements (PFR) rule change request. As an active investor in energy markets across Australia, we own and contract a generation portfolio of nearly 3,000MW and provide retail energy supply to more than 1.1 million electricity and gas customers. Further, Alinta Energy is a provider of mandatory narrow band PFR and is therefore well placed to comment on the draft determination.

Maintaining the stability of essential system services, including frequency response is critical to the operation of the power system. Historically these services have been provided as a bi-product of energy production by large synchronous generation. However, as foreshadowed by the Energy Security Board's final Post 2025 Review of the NEM report, the retirement of incumbent large generation and the influx of an unprecedented level of renewable generation, hydro generation and energy storage is signaling the 'changing of the guard'. What worked during the early years of the NEM and the decades that followed, can no longer be relied on to provide these power system services today. This same principle is equally applicable to PFR services.

Alinta Energy acknowledges the rationale for AEMC's final rule in 2020 to reintroduce compulsory PFR for all scheduled and semi schedule generators combined with a sunset date and further review of the enduring arrangements. We accepted this rule on the basis that a rapid increase in PFR provision was necessary to support the energy market transition in the interim while a more enduring market based approach was designed. We are therefore deeply disappointed that this draft determination sets out a plan to continue mandatory narrow band PFR on an enduring basis and remove the sunset clause.

Alinta Energy does not support this draft determination. The key decisions appear rushed and are very different from the direction previously discussed with industry. In addition, the high level design of the corresponding incentives and double-sided causer pays frameworks are complex and require further explanation and clarity on its intended practical operation.

We have detailed out our mains concerns below further:

1. Role of enduring mandatory PFR

As above, Alinta Energy understood the interim mandatory role for PFR as a placeholder

to accommodate immediate impacts to frequency resulting from changes to the generation mix across the NEM and that the sunset period was to be used to develop an enduring alternative market based arrangement or similar. Indeed, while we are not a participant on the AEMC's PFR Technical Work Group (PFR TWG), we also understood that this was the intended enduring direction (in some form) that was being discussed with the working group, in line with the ESB's positioning on 'valuing missing markets'. However, the draft determination presents a very different and unpalatable approach, supported largely by AEMO as technical advisers and backed up (in part) by independent consultants. While it appears simple and cost-efficient to continue to mandate PFR and remove the sunset clause, this approach fails to provide a suitable longer term investment signal to adequately incentivise voluntary PFR into the future.

We note that the AEMC's independent consultant, GHD, in part, agreed that a key risk with this model is that without a suitable incentive regime, the same PFR problems pre the 2020 final rule would likely reoccur following the retirement of incumbent synchronous (thermal) generation. In their words, GHD postulated:

*"Looking further ahead, we see that there may be a need to establish stronger market arrangements that provide a greater level of certainty for system operation and send the right price signals to the market for provision of future PFR capacity (reserves), particularly in the lead up to the retirement of a large number of the NEM's coal fired generating fleet at the end of this decade, and beyond.....The importance of ensuring sufficient PFR reserve is available cannot be understated and hence there is a need to value it."*¹

In Alinta Energy's view, development of the market arrangements outlined by GHD will take some time to design and implement by the late 2020's. We therefore strongly encourage the AEMC to revise its draft determination by reconsidering (in conjunction with its PFR TWG and via broader stakeholder consultation) the best way to value PFR provision. In the meantime the sunset clause should be extended until a pathway to a suitable market arrangement has been established.

2. Lack of transparency has increased sovereign risk

Alinta Energy is concerned with the differing discussions that have been held with AEMO and the industry, including the TWG. As above, our understanding was that the AEMC and its TWG had been working collaboratively and constructively together to design a suitable market arrangement and incentive regime.

Alinta Energy also notes that in good faith, generators in the NEM may have decided to defer an PFR exemption application or undertake further investment (such as retrofitting for improved PFR capability) based on previous policy positions presented by the AEMC in its 2020 final report, its December 2020 Directions Paper and the ESB's Post 2025 Review of the NEM recommendation on ESS markets. Specifically, the AEMC's view in its December 2020 paper stated²:

"The initial position is that pathway two [Revise the Mandatory PFR arrangement by widening the frequency response band and develop new FCAS arrangements for the provision of PFR during normal operation] is likely to provide a balance between providing operational certainty and system resilience while incorporating new market arrangements that are likely to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of electricity consumers. The

¹ https://www.aemc.gov.au/sites/default/files/2021-09/GHD_Enduring%20Primary%20Frequency%20Response%20Final%20Report%20Final.pdf; page ii

² <https://www.aemc.gov.au/sites/default/files/2020-12/Frequency%20control%20rule%20changes%20-%20Directions%20paper%20-%20December%202020.pdf>

arrangements under pathway two incorporate elements of both mandatory and market-based procurement, albeit for different types of PFR. While further detailed policy development is required, this hybrid approach would provide AEMO with additional operational tools and is likely to provide greater flexibility to future power system developments ".

We are therefore disappointed that the AEMC have decided to pursue an enduring compulsory narrow band PFR arrangement instead and are further surprised that it has developed a complex high-level frequency performance payment mechanic without testing this with industry or developing any detailed explanatory modelling.

3. Untested payment mechanism and 'evolved' causer pays framework

Our initial understanding of this payment performance mechanic is that there are likely limited times in which positive payments would be realised. However, we also acknowledge that we have had insufficient time to fully understand and test how it would operate in practice. The same is true for the proposed 'double-sided causer pays framework' (DSCP).

At first glance, and in conjunction with the lower-probability of triggering the payment mechanism, it appears the DSCP may leave the majority of generators in a worse position compared to the status quo because cost recovery would be smeared.

Noting the complexities of the frequency performance mechanism and the lack of broader detail around the DSCP framework, Alinta Energy strongly encourages the AEMC to undertake further stakeholder consultation to better explain (and further develop) the policy design, instead of leaving this design work to AEMO. Should it decide to continue with the approach set out in its Draft Determination, we would welcome a delay to the final determination and the addition of a further consultation paper focusing on the payment incentive mechanic and DSCP framework.

4. Clarity of objective and role of Reliability Panel unclear

As a frequency service in the NEM, it appears prudent that the Reliability Panel provides expert advice on the objective of PFR provision and how it should best be delivered. However, it is not clear if their advice has been sought.

Alinta Energy encourages the AEMC to seek the views of the Reliability Panel on any forward arrangement. At a minimum, the Reliability Panel should assess whether the Frequency Operating Standard requires changes to accommodate the Draft Determination, and their views should be sought on ways to encourage long term voluntary PFR capability.

Should you wish to discuss our views further, please contact me on 0475 943 365 or at Dan.Mascarenhas@alintaenergy.com.au.

Yours Sincerely

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