
Australian Energy Market Commission

DRAFT REPORT

**REVIEW OF THE OPERATION OF THE
RETAILER RELIABILITY OBLIGATION**

28 SEPTEMBER 2023

REVIEW

INQUIRIES

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ABOUT THE AEMC

The AEMC reports to the energy ministers. We have two functions. We make and amend the national electricity, gas and energy retail rules and conduct independent reviews for the energy ministers.

ACKNOWLEDGEMENT OF COUNTRY

The AEMC acknowledges and shows respect for the traditional custodians of the many different lands across Australia on which we all live and work. We pay respect to all Elders past and present and the continuing connection of Aboriginal and Torres Strait Islander peoples to Country. The AEMC office is located on the land traditionally owned by the Gadigal people of the Eora nation.

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SUMMARY

- 1 The Australian Energy Market Commission (the AEMC or Commission) is making draft recommendations to improve the operation of the Retailer Reliability Obligation (RRO).
- 2 The review of the operation of the RRO is being carried out in the context of the national electricity market (NEM) undergoing a significant transformation. It is shifting from a capacity-limited thermal power system to a more energy-limited power system characterised by high levels of variable renewable energy (VRE). The transformation requires careful consideration of how reliability is characterised and managed to continue to ensure the system can meet customer demand at a level they value. The Commission considers that the policy rationale remains for mechanisms such as the RRO to support firming capacity and market liquidity in the NEM in the transition.
- 3 In light of this, the Commission has carefully considered submissions to the review and is making fourteen draft recommendations to ensure the RRO operates effectively and contributes to the national electricity objective (NEO). The recommended changes are designed to improve the operational efficiency of the RRO by reducing regulatory burden for market participants and reducing costs for consumers.
- 4 The RRO is designed as a long term mechanism with obligations placed on market generators to improve market liquidity and liable entities to invest in firmed generation in periods where reliability gaps are identified in regions. It is one of several measures aimed at supporting reliability in the NEM. It commenced on 1 July 2019, with the aim of providing '*stronger incentives for market participants to invest in the right technologies in regions where it is needed, to support reliability in the NEM*'.¹
- 5 The RRO forms part of the overall reliability framework in the NEM and is designed to complement the reliability standard and market price settings, including the market price cap, cumulative price threshold, administered price cap and market floor price.

The SA T-1 trigger identified a number of opportunities for reform

- 6 The RRO has only been triggered once at T-1 with compliance processes still underway with the South Australian (SA) T-1 Reliability Instrument for the period 8 January 2024 to 29 February 2024.
- 7 Submissions to the review raised concerns that the operation of the RRO through the National Electricity Law (NEL), National Electricity Rules (NER) and RRO guidelines – in respect to the SA T-1 Reliability Instrument – had resulted in regulatory burden and additional costs which will be borne by consumers, while not delivering additional reliability to meet the interim reliability measure (IRM).
- 8 Specifically submissions noted that at the time the consultation paper was released in March 2023, the reliability gap in the Australian Energy Market Operator (AEMO) 2022 Electricity Statement of Opportunities (ESOO) Update was no longer below the IRM threshold, and

¹ AER, Retailer Reliability Obligation, found [here](#).

advanced projects being developed in time for the gap period were unable to be effectively accounted for in net contract position (NCP) compliance.² Submissions argued that this meant additional contracting occurred which was not needed to address the reliability gap and at higher cost. Other submissions also argued to expand the types of eligible qualifying contracts to include more demand response contract types to reduce costs while still meeting the policy intent of addressing the reliability gap.

9 The Commission notes that while the SA T-1 reliability gap was no longer below the IRM threshold in the 2022 ESOO update, it was subsequently re-established in the 2023 ESOO released in August 2023.³

10 The Commission agrees that some definitions in the NEL and NER may have led to some inefficient outcomes for the market and consumers which do not contribute to the NEO. The Commission is making recommendations in the draft report to address these issues.

The Commission has made draft recommendations to improve the operation of the RRO

11 The Commission is making fourteen draft recommendations to the operation of the RRO. These changes are designed to improve operational efficiency by reducing regulatory burden for market participants and reducing costs for consumers.

12 In summary, the draft recommendations are to:

- Move the T-1 NCP compliance date to T and continue ex-post compliance testing only if a reliability gap occurs, to reduce regulatory burden and costs for consumers (recommendation 1).
- Change AEMO's reliability gap forecasting timeframes to ensure that reliability instruments are made with the best available information and cover potential gaps throughout the year (recommendation 2).
- Remove the voluntary book build mechanism, which is not being used, to simplify the NEL and NER (recommendation 6).
- Improve the overall operation of the MLO for market participants in the short term (recommendation 5), while noting that over the longer term, the MLO could be further reviewed.
- Make changes to the NEL and NER and review guidelines to address a number of operational issues raised in submissions to reduce regulatory burden and deliver lower costs opportunities for compliance (recommendations 3 and 7 to 14).

13 The Commission also proposes a number recommendations for minor corrections to the NEL and NER where stakeholders have identified minor amendments (including amending 4A.D.6 to correct a reference from megawatts (MW) to percentage (%)).

14 The Commission considers that these draft recommendations will better balance support for

² AEMO, Update to 2022 Electricity Statement of Opportunities, February 2023.

³ AEMO, 2023 Electricity Statement of Opportunities, August 2023.

reliability outcomes as the NEM transitions and reduced regulatory burden and cost for consumers.

- 15 The RRO is implemented through the NEL and NER as well as detailed guidelines developed by AEMO and AER. This means that there are likely to be different lead times on when reforms can be implemented. In particular, three of the draft recommendations (recommendations 1, 2 and 3) would require legislative amendments that would need to be approved by the Energy Ministers Sub-Group and passed by the South Australian Parliament. Where the AEMC has recommended changes to guidelines, the AEMC recommends that changes be made following reviews by AEMO and AER of these guidelines.

The draft recommendations contribute to the NEO

- 16 The draft recommendations contribute to the NEO by ensuring the RRO operates more effectively by reducing regulatory burden for liable entities and reducing costs for consumers:
- Changing the compliance date from T-1 to T will improve operational efficiency by reducing regulatory burden if a gap is closed between T-1 and T. Moving the date from T-1 to T, while still maintaining T-1 as the notification date, will improve incentives for liable entities to contract with firmed generation and demand side management. It will also enable liable entities to better align compliance requirements with actual demand, reducing the risk of over or under-contracting.
 - Changing processes for initiating T-3 and T-1 triggers will reduce the complexity for reliability instrument requests by AEMO and enable AEMO to request the removal of a T-1 instrument, under limited circumstances, if a gap is removed in an ESOO Update between T-1 and T.
 - Removing the voluntary book build mechanism reduces regulatory burden by removing an aspect of the RRO that is not being used. Maintaining key aspects of the RRO including definitions for liable entities and MLO groups and the respective role of the AER will support stability and predictability.
 - Reviewing aspects of the RRO including the eligibility of qualifying contract types with a firmness of 1 and demand side management will enable more practical compliance for liable entities.

Some reforms suggested would not best contribute to the NEO

- 17 The Commission has recommended against expanding AER powers to override or reassess an AEMO reliability instrument request (recommendation 4) as not contributing to the NEO.
- 18 The Commission has also considered the option of not making further changes to the RRO or making minor changes, and reviewing the RRO after more information becomes available on how it is operating in practice and following further T-1 events. However, the Commission considers that the recent experience with the SA T-1 trigger event shows that changes to the NEL and NER are in the interests of consumers and market participants to reduce regulatory burden and costs.

The context in which the RRO is operating is quickly evolving

- 19 The Commission acknowledges that a significant transition is underway in the NEM.
- 20 Since the introduction of the RRO in 2019, there have been changes in policy levers to incentivise firm generation. The review of the form of the reliability standard has commenced, the Commonwealth Government's Capacity Investment Scheme (CIS) is under development and a number of jurisdictional schemes are underway including the NSW Electricity Infrastructure Roadmap. These mechanisms may overlap or duplicate elements of the RRO in the future and, once further details are known of these mechanisms, further consideration of their overlap with and policy intent of the RRO may be warranted.
- 21 There have also been a number of reviews – including by the Australian Competition and Consumer Commission (ACCC), Energy Security Board (ESB) and AEMC – into market liquidity in the NEM since 2018. The outcome of these reviews led to the introduction of the MLO and additional measures including expanding AER market monitoring powers.
- 22 In addition to the fourteen recommendations, the AEMC may consider self-initiated reviews of the overall policy efficiency of the RRO and market liquidity, taking into account new policy mechanisms which may overlap with the operation of the RRO.

We are seeking feedback on the draft recommendations

- 23 The Commission encourages stakeholders to provide feedback on the Review's analysis and recommendations. Submissions are due by 2 November 2023. The Commission expects to release its final report in February 2024.
- 24 Changes recommended may require changes to the NEL and NER. The Commission's draft recommendations are presented below in Box 1.

BOX 1: DRAFT RECOMMENDATIONS

The Commission is making fourteen draft recommendations across areas identified in the consultation paper to improve the operation of the RRO.

PROCESS FOR T-3 AND T-1 TRIGGERS

Recommendation 1: Move the T-1 Net Contract Position (NCP) compliance date to T and continue ex-post testing only if a reliability gap occurs, to reduce regulatory burden and better enable newly committed project contracts to be used to comply with a reliability gap.

Recommendation 2: Provide AEMO with a limited power to request the AER cancel a T-1 reliability instrument following an Electricity Statement of Opportunity (ESOO) or ESOO Update between T-1 and T which shows a reliability gap has closed.

Recommendation 3: Change the timeframe for AEMO to request a reliability instrument from 3 to 9-months, to provide greater flexibility when AEMO can request a reliability instrument including better taking into account ESOO Updates which may subsequently close

a reliability gap.

Recommendation 4: Maintain the AER's existing role in assessing reliability instrument gap requests to ensure a clear differentiation in roles of market bodies.

MARKET LIQUIDITY OBLIGATION

Recommendation 5: Amend the MLO from a 15 per cent threshold for MLO groups to 10 per cent threshold to ensure that the MLO continues to support market liquidity in South Australia (SA).

VOLUNTARY BOOK BUILD MECHANISM

Recommendation 6: Remove the voluntary book build mechanism, which is not being used, to simplify the NEL and NER.

QUALIFYING CONTRACTS

Recommendation 7: The AER review expanding eligible demand-side management contract types to increase the pool of eligible contracts, to reduce cost and regulatory burden for liable entities.

Recommendation 8: AEMO review expanding timeframes for the AEMO demand portal being open to expand the pool of eligible demand response contracts and reduce costs.

Recommendation 9: The AER review the contracts and firmness guidelines to expand eligibility of qualifying contracts with a firmness of 1 to include caps above 5% of the Market Price Cap to increase the pool of eligible contracts and reduce costs.

Recommendation 10: The AER review opportunities to simplify bespoke methodology and audit arrangements through its guidelines, taking into account the experience of liable entities with the SA T-1 event, to reduce costs for compliance.

LIABLE ENTITIES

Recommendation 11: Maintain the timeframes for advice on procurer of last resort (PoLR) costs, and instead progress with simplifying compliance through changing the NCP compliance date from T-1 to T.

Recommendation 12: Maintain the existing role of market customers as liable entities.

OPT-IN MECHANISM

Recommendation 13: Maintain the existing opt-in mechanism arrangements.

COMPLIANCE PROCESSES

Recommendation 14: The AER review options to simplify compliance arrangements through guidelines.

HOW TO MAKE A SUBMISSION

We encourage you to make a submission

Stakeholders can help shape the solution by participating in the review. Engaging with stakeholders helps us understand the potential impacts of our recommendations and contributes to well-informed, high quality reforms. We encourage stakeholders to provide feedback on the Review's analysis and recommendations.

How to make a written submission

Due date: Written submissions responding to this draft report must be lodged with Commission by **2 November 2023**.

How to make a submission: Go to the Commission's website, www.aemc.gov.au, find the "lodge a submission" function under the "Contact Us" tab, and select the project reference code **EPR0091**.⁴

Publication: The Commission publishes submissions on its website. However, we will not publish parts of a submission that we agree are confidential or that we consider inappropriate (for example offensive or defamatory content or content that is likely to infringe intellectual property rights).⁵

For more information, you can contact us

Please contact the project leader with questions or feedback at any stage.

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⁴ If you are not able to lodge a submission online, please contact us and we will provide instructions for alternative methods to lodge the submission

⁵ Further information is available here: <https://www.aemc.gov.au/contact-us/lodge-submission>

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1 THE COMMISSION HAS CONSIDERED THE CONTEXT FOR THE RRO

The retailer reliability obligation (RRO) supports investment in firmed generation by requiring liable entities (largely retailers) to obtain contracts that cover their expected demand during reliability gap periods. This, in turn, is intended to provide market participants with the necessary confidence to invest in firmed generation and demand side management to support a reliable electricity supply in the national electricity market (NEM).

Clause 11.116.18 of the National Electricity Rules (NER) requires that the Commission review the operation of Chapter 4A - RRO. The terms of reference of the review set out that the:

- Commission will consider certain aspects of the operation of the RRO to ensure that the scheme is operating as intended
- Energy Security Board (ESB) decision Regulatory Impact Statement (RIS) for the RRO outlined that the intent of this review is not to assess the overall efficiency of the RRO, as determining the overall impact of the scheme would require a longer horizon.

1.1 The policy rationale for the RRO remains

The RRO was introduced to support the reliability framework in the NEM in order to:⁶

Encourage new investment in dispatchable energy such that the electricity system operates reliably.

This was in the context of:⁷

The reduction in dispatchable coal and gas generation and the greater penetration of intermittent technologies such as solar and wind generation present risks to the NEM's reliability.

When introduced, the RRO was intended to be a longer-term solution to ensuring reliability at the lowest cost by preparing for and eliminating forecast reliability gaps before they occur.

As the market transitions to increasing variable renewable energy and the retirement of thermal generation, the nature of reliability risk continues to change. Due to continuing concerns around these risks, the Reliability Panel (the Panel) is considering if a new form of the reliability standard is needed to incentivise investment. The Commonwealth Government is also developing a Capacity Investment Scheme (CIS) through competitive tenders seeking bids for clean renewable generation and storage projects to fill expected reliability gaps and jurisdictional measures are under development including the NSW Energy Infrastructure Roadmap.

⁶ Energy Security Board, Retailer Reliability Obligation Decision Regulation Impact Statement, 19 December 2018.

⁷ Ibid.

While these measures are still being developed, the Commission considers the RRO plays a role in supporting new investment in, and contracting for, firm generation in periods of forecast reliability gaps.

1.1.1

Stakeholders argued the review should cover the policy efficiency of the RRO

In its submission, the Australian Financial Market Association (AFMA) argued, *'In AFMA's view it is a flawed mechanism that is unlikely to contribute meaningfully to system reliability and should be replaced. The fundamental flaw of the RRO is that it attempts to deal with the lack of physical dispatchable capacity by mandating retailers enter into an inefficient level of contracting in the financial market.'*⁸

SEA Gas argued for the assessment framework to be expanded to consider the robustness of the physical supply chain to meeting obligations under the RRO.⁹

The AEC and Delta Electricity argued that the consultation paper was unclear on whether AEMC will consider the policy efficiency of the RRO. Delta Electricity also argued that the administrative burden be considered within the simplicity and transparency assessment criteria.¹⁰

Three submissions also argued for the terms of reference to be expanded to consider the Ministerial T-3 trigger.¹¹

1.1.2

Our draft position is that the existing terms of reference are appropriate

The RRO is still a new mechanism that has been triggered on six occasions at T-3 and on one occasion at T-1 as of September 2023¹². As set out in this report, the Commission considers there are opportunities to improve the operation of the RRO to ensure that it is better meeting its original policy intent. We also consider that risks to reliability may continue in the transition to a high variable renewable energy (VRE), energy-limited power system. Maintaining a predictable, reliable and stable system in the transition supports the NEO.

Further, given the AER has only recently made its first T-1 reliability instrument, there is limited data and experience to determine the overall policy efficacy, and alternative mechanisms are not yet in place to compare reliability outcomes.

The market would need to have multiple instances of T-1 trigger events to allow us to determine the overall policy efficiency of the RRO. Further, the Ministerial T-3 trigger for all jurisdictions has only recently been put in place and there is insufficient information available to determine its effectiveness in supporting market liquidity.

8 Submission to the consultation paper: AFMA p.1.

9 Submission to the consultation paper: Origin p.1.

10 Submission to the consultation paper: Delta Energy, p.1.

11 Submissions to the consultation paper: AFMA, EUAA and SA Water.

12 Two further T-3 reliability instrument requests are being considered by the AER [link](#)

1.2 The NEL and NER should better support decisions based on new information

The RRO is new, having commenced on 1 July 2019, and market bodies are continuing to work with market participants on its effective operation.

In some instances, market bodies may have been restricted under the NER and NEL in their ability to make decisions based on new information when it became available, potentially leading to higher costs and regulatory burden which may have not been needed to address reliability gaps.

The SA T-1 trigger event timeline, described in appendix A, highlights a number of issues that appeared throughout 2022 and 2023 and responses by market bodies to address issues in accordance with the NEL and NER.

Issues around using the Australian Energy Market Operator (AEMO) Electricity Statement of Opportunities (ESOO) methodology for forecasting reliability gaps were highlighted by stakeholders in 2022. In April 2023, AEMO updated its NEM Reliability Forecasting Guidelines and Methodology to include 'anticipated projects' in forecasts from the 2023 ESOO. This is expected to provide more up to date reliability gap forecasts.

Submissions argued that delays in finding resolutions (specifically aligning the AEMO reliability gap methodology more closely with updated timeframes for project delivery) resulted in the SA T-1 event being unnecessarily triggered. Consequentially, stakeholders argue this led to higher costs being borne by consumers and liable entities through complying with the T-1 reliability gap and not being able to add newly committed projects to comply with net contract position (NCP) requirements, such as the Bolivar power station and batteries at Taillem Bend and Torrens Island.

The AEMC notes that forecasting reliability gaps is subject to uncertainty and change, including changes in the opening and closure of generation assets and changes in seasonal demand forecasts.

The 2023 ESOO again shows that the reliability gap for the SA T-1 remains above the IRM threshold.

While some issues are likely to be resolved going forward, such as through changes to the methodology used by AEMO to forecast T-3 reliability gaps, these changes were not in place at the time of the SA T-1 reliability gap trigger event. The methodology changes should mean that T-3 triggers initiated by an ESOO are less likely in the future as forecasts take into account anticipated projects.

1.3 A further review could consider the overall policy efficiency of the RRO

Since the RRO policy was developed, a number of changes to electricity market arrangements have been introduced or are proposed which may overlap with the RRO. These include the Panel's consideration of a possible new form of the reliability standard commencing from 1 July 2028, the extension of the IRM to 30 June 2028, and several new

measures being developed by Commonwealth and jurisdictional governments, such as the CIS and the NSW Electricity Infrastructure Roadmap.

The Commission agrees that it may be necessary to consider the RRO policy in light of the overlap in these additional policy mechanisms, once they are in place, to support efficient investment in the NEM and to contribute to simplicity and transparency under the NEO. However, it is too early to review the overall policy effectiveness of the RRO until after these mechanisms have been further developed.

2 THE COMMISSION HAS MADE DRAFT RECOMMENDATIONS

This draft report makes fourteen draft recommendations for the operation of the RRO.

In the consultation paper, the Commission sought stakeholder feedback on questions covering the proposed assessment framework, process for T-3 and T-1 triggers, the market liquidity obligation (MLO), voluntary book build mechanism, liable entity requirements, qualifying contacts opt-in and compliance processes.

As set out in this report, the Commission has relied on information provided in the submissions as well as a range of additional information and data.

The Commission has also considered the option of not making further changes to the RRO and instead considering a review after more information becomes available on how the RRO has operated. However, as noted previously, the Commission considers that the recent experience with the SA T-1 trigger event shows that changes to the NEL and NER are in the interests of consumers and market participants and contribute to the NEO by reducing regulatory burden and costs to consumers.

This chapter sets out the Commission's considerations of the issues, responses to submissions and the Commission's draft recommendations.

The Commission recognises that the fourteen recommendations may require changes to the NEL, NER and guidelines. Changes to the NEL and NER will require longer timeframes to implement than amendments to existing guidelines.

2.1 Our recommendations are designed to improve the RRO

The Commission considers that the RRO can be simplified to ensure it is more effectively delivering upon its policy intent and to reduce regulatory burden and costs.

The RRO is implemented through a complex set of laws, rules, guidelines and procedures that amount to several hundred pages of detailed guidance for market participants, including:

- Part 2A and section 90EA of the National Electricity Law
- Chapter 4A and Parts ZZZR and ZZZZH in Chapter 11 of the National Electricity Rules
- Nine guidelines released by the AER and AEMO.

The operational complexity of the RRO is designed to ensure that the policy intent is met to the greatest extent possible, with civil penalties for non-compliance.

The Commission considers that opportunities to simplify the operation of the RRO without fundamentally changing the overall policy intent should be prioritised as reforms.

2.2 A range of information shaped our recommendations

The Commission received sixteen submissions in response to the consultation paper. Submissions argued that the complexity of the RRO is not delivering the best outcomes in terms of regulatory burden, reliability outcomes and costs for consumers.

Fourteen submissions recommended changes to improve the operation of the RRO or simplify processes.

Five submissions indicated a preference that the terms of reference be expanded to consider the efficacy of the RRO or that the RRO was instead repealed when the Commonwealth Government's CIS commences.¹³

The submissions recommended around 60 changes, with a number of changes overlapping. These changes represent numerous options to change the operation of the RRO to ensure it is meeting its policy intent, reduce the regulatory and cost burden for liable entities, simplify procedures for market bodies and reduce costs to consumers.

Mr Geiser¹⁴ and the Public Interest Advocacy Centre (PIAC) argued that the RRO should be repealed.

In making its draft recommendations, the Commission has considered feedback from submissions as well as a number of other sources of information including ASX Energy data, prices in the NEM pre and post reliability instrument periods and information provided in the 2022 ESOO, 2022 ESOO Update and 2023 ESOO.

The AEMC is continuing to explore stakeholders' compliance experience with the SA T-1 NCP reporting on 31 July 2023. Further information may also become available if obligations are triggered during the SA T-1 gap period between 8 February 2024 to 29 February 2024.

Following the publication of the consultation paper, AEMO and the AER released two documents which address issues raised in submissions around the RRO:

- In April 2023, AEMO released its final report for the reliability forecasting guidelines and methodologies consultation which extends the application of 'anticipated' projects to RRO forecasting¹⁵
- In June 2023, the AER released the RRO Reliability Compliance Procedures and Guidelines – Final which sets out final decisions on compliance arrangements for liable entities under the RRO including audits and policies, systems and procedures that regulated entities must establish.¹⁶

The Commission also recognises that there is more information available on the operation of the RRO at T-3 than at T-1, given that at August 2023, T-3 reliability instruments have been issued on six occasions and a T-1 reliability instrument has only been issued once at September 2023.¹⁷

13 Submissions to the consultation paper: AEC, AFMA, EnergyAustralia, ENGIE and Shell Energy.

14 Who made a submission as a private individual.

15 AEMO, Reliability Forecasting Guidelines and Methodologies Consultation Final Report, 24 April 2023, found [here](#).

16 AER, Reliability Compliance Procedures and Guidelines - Final Decision, June 2023, found [here](#).

17 AER, Register of Reliability Instruments.

AEMO has recently made two new T-3 Reliability instrument requests to the AER¹⁸ and may make further requests taking into account the 2023 ESOO and the rule change to extend the IRM.

The AEMC has also made a rule change to extend the interim reliability measure (IRM) to 30 June 2028.¹⁹

2.3 We are making draft recommendations to change the T-3 and T-1 processes

The Commission sought stakeholder feedback on the process for the T-3 and T-1 triggers for the RRO. We are making draft recommendations to:

- move the NCP compliance date from T-1 to T while maintaining T-1 as a notification date
- provide AEMO with a limited power to request the AER to remove a T-1 trigger if a gap has closed between T-1 and T
- change the timeline for when AEMO can request a trigger event from 3 to 9-months to better take into account winter or shoulder period reliability gaps.

These three draft recommendations would require amendments to the NEL as well as amendments to the NER. For example, moving the NCP compliance date would require amendments to section 14H(b)(i) of the NEL and a number of clauses in the NER.

Some stakeholders argued that the AER should have greater powers to refuse or over ride a reliability instrument request. The Commission's draft recommendation is not to extend the AER's powers. Doing so would not contribute to the NEO as it could lead to uncertainty around market operations and the respective roles of different market bodies.

Further, information on the recommendations are outlined below.

2.3.1 Moving the NCP date from T-1 to T to reduce regulatory burden

DRAFT RECOMMENDATION 1: MOVE THE T-1 NCP DATE TO T

Moving the T-1 NCP compliance date to T and continue ex-post testing only if a reliability gap occurs, will reduce regulatory burden and better enable newly committed project contracts to be used to comply with a reliability gap.

The NCP is fundamental to the operation of the RRO, requiring liable entities to pre-qualify contracts for a future gap period – incurring costs upfront and potentially again if a gap occurs.

NCP arrangements at T-1 are defined in section 14O of the NEL including the requirement for a reliability instrument to include the NCP date at T-1 and the reporting date.

¹⁸ Link [here](#).

¹⁹ AEMC, Extension of the application of the IRM to the RRO - Final determination, 21 September 2023.

Section 140 of the NEL establishes that a liable entity's NCP during a particular period is:

- the number of MW of electricity to which the liable entity's qualifying contracts relate for the period; and
- adjusted in accordance with the NER to account for the likelihood that, despite the qualifying contracts, the liable entity retains exposure in relation to the volatility of the spot price during the period.

The NCP is further defined in clause 4A.E.2 of the NER, with dates established in specific reliability instruments.

The RRO decision Regulatory Impact Statement establishes that the NCP date was set at T-1 to ensure liable entities had contracted well in advance of a reliability gap.

However, it has several limitations identified in submissions.

1. Liable entities may not be able to contract with certainty with newly built projects which may be commissioned between T-1 and T²⁰
2. Liable entities may not know of their expected demand at T-1 which may lead to over or under contracting²¹
3. Audit and compliance costs may be unnecessary if an instrument is withdrawn or the gap does not occur. The AER faces a significant task in assessing gaps for all periods in a reliability instrument if 50 per cent Probability of Exceedance (PoE) is triggered.

The Commission agrees with stakeholders that there are benefits in moving the NCP date from T-1 to T. The Commission considers that the change contributes to the NEO by supporting operational efficiency and providing appropriate incentives to invest in firm capacity in a timely manner. The Commission considers that maintaining T-1 as a notification date will continue to achieve the policy intent of the RRO to incentivise early contracting given the penalties and costs in place if a liable entity does not report sufficient contracts for a 50 per cent PoE at T.

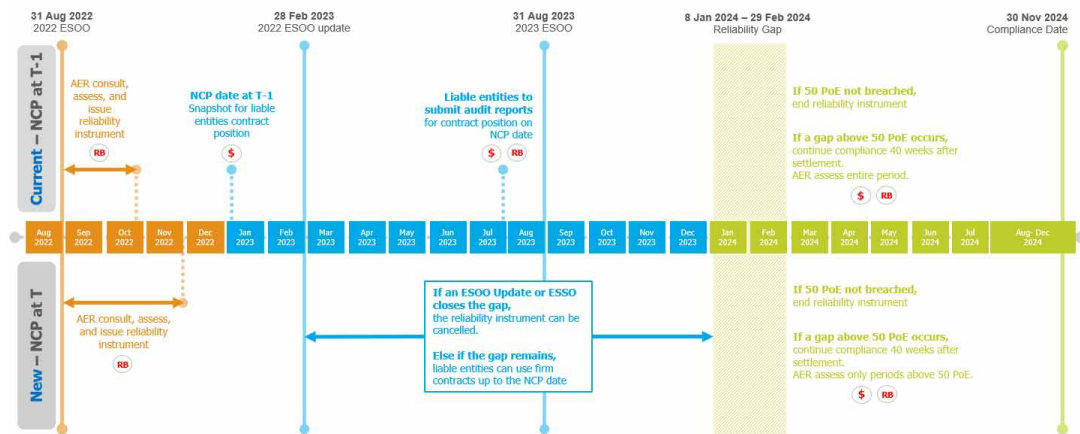
The Commission acknowledges there are potential implications of moving the NCP date to T. Specifically the AER and liable entities will have later advice on contracting (including pre-qualification and compliance). However, the AER wholesale market monitoring powers will continue and the existing RRO penalty arrangements will set a strong compliance signal with the RRO. Liable entities will also have more time to submit bespoke methodologies to independent auditors.

The Commission still considers that contracting a year out from a reliability gap is important to the policy intent of the RRO. As noted above, the Commission therefore recommends maintaining T-1 as a notification date but moving the T-1 NCP compliance date to T, and continuing ex-post testing only for those periods where a reliability gap occurs Figure 2.1.

20 Submission to the consultation paper: Origin Energy, pg 3.

21 Submissions to the consultation paper: Shell Energy, p. 2.

Figure 2.1: Example - how a change of an NCP date at T-1 to T would have applied to the SA T-1 event



2.3.2

Changing timelines for AEMO reliability instrument requests from 3 to 9 months

DRAFT RECOMMENDATION 2: CHANGE THE TIMEFRAME FOR AEMO TO REQUEST A RELIABILITY INSTRUMENT FROM 3 TO 9-MONTHS

This will provide greater flexibility when AEMO can request a reliability instrument including better taking into account ESOO updates which may subsequently close a reliability gap.

The Commission considers that changing the timeframe for AEMO to make a reliability instrument request from 3 to 9-months will enable AEMO to effectively cover potential reliability gaps in spring and autumn periods and ensure that AEMO is able to consider new information which may subsequently close a gap.

In its submission, AEMO argued that the timeframe for making a reliability request to the AER be extended to 9-months to limit inefficiencies and risk of an increasing number of ESOO updates and better align with the changing nature of reliability risk.²²

Timeframes for AEMO to request a reliability instrument and the AER to assess and respond are prescribed in the NEL and NER.²³ Figure 2.2 shows these timelines in relation to the NCP date for an example summer gap.

The timelines are effective for summer gaps that are forecast in an August ESOO, however constrain the ability for AEMO to make gap requests in spring and autumn.

²² Submission to consultation paper: AEMO, p.3.

²³ Section 14H of the NEL; clause 4A.C of the NER.

The Commission agrees that under the NEL and NER, the timeframes to issue and comply with a reliability gap are complex, constrain when decisions can be made by the AEMO and the AER and impact decisions by liable entities MLO generators.

For example, AEMO must publish the reliability gap in an ESOO or ESOO Update no more than 42-months prior to the forecast gap and submit a T-3 request no less than 39-months prior.²⁴ This gives AEMO three months to publish a forecast gap and submit a request for a T-3 instrument. The AER must make a determination on a reliability instrument within two months of receiving a request.

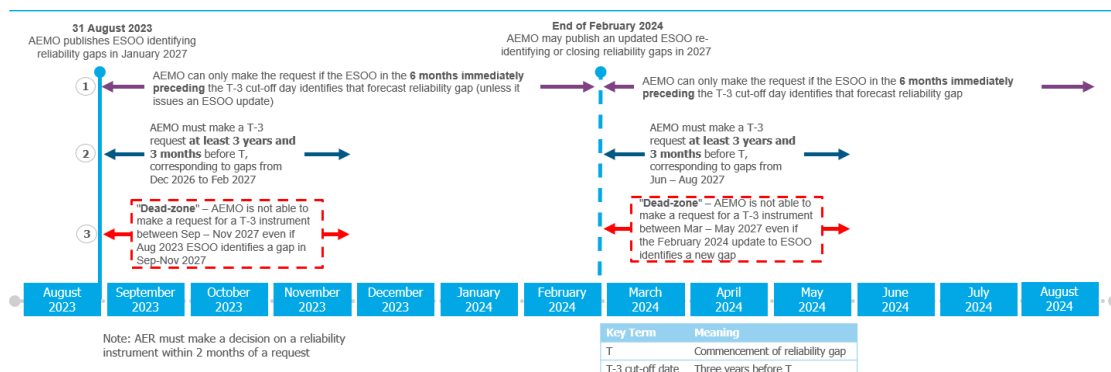
The Commission considers that the timeline of 3-months is too short and leaves 'dead-zones' in spring and autumn where reliability instruments are not able to be made if a gap appears. These timelines do not best contribute to the NEO as they impose unnecessary complexity and may limit AEMO's ability to make reliability instrument requests as the NEM transitions.

Figure 2.2 and Figure 2.3 shows how extending timeframes for AEMO to request an instrument to 9-months removes 'dead-zone' periods and enables AEMO to hold off making a request until later and potentially taking account of new projects. Along with changing the NCP date from T-1 to T, these measures together also extend the window for liable entities to contract with new projects.

This change also recognises that in April 2023, AEMO announced a change its reliability forecasting methodology to capture 'anticipated' projects from the 2023 ESOO. This is a decision for AEMO in its guidance to the market, rather than through changes to the NEL or NER, and will ensure more recent data can be considered in reliability gap forecasts.

In relation to enabling AEMO to request multiple gaps in a year, the Commission considers the current arrangements effectively contribute to the NEO.

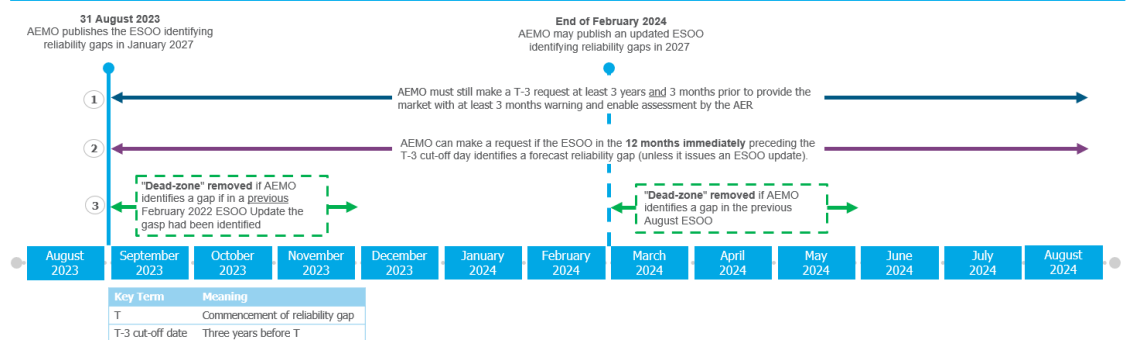
Figure 2.2: Existing RRO T-3 timeline - stylised for a 2027 reliability gap



Source: AEMC

24 Clause 4A.C.2 of the NER.

Figure 2.3: Proposed new RRO T-3 timeline - stylised for a 2027 reliability gap



Source: AEMC

2.3.3

Providing AEMO with a limited power to request the removal of a reliability instrument

DRAFT RECOMMENDATION 3: PROVIDE AEMO WITH A LIMITED POWER TO REQUEST THE AER REMOVES A T-1 INSTRUMENT

Providing AEMO with a limited power to request the AER remove a T-1 reliability instrument following an ESOO Update between T-1 and T which shows a reliability gap has closed supports certainty.

AEMO's role in establishing a reliability instrument by making a request to the AER is set in the NEL and NER. AEMO is unable to request to withdraw a reliability instrument once the NCP date has passed.

Moving the NCP date from T-1 to T will address many of the issues raised by stakeholders in their submissions including by ensuring contracts with newly committed projects can be used with more certainty by liable entities to comply with a reliability gap.

However, a new limited power that enables the AEMO to request the removal of a reliability instrument post a T-1 date if an ESOO or ESOO Update closes the gap between the T-1 and the reliability gap period could be implemented to formally close a reliability instrument before T.

The Commission recommends that this power is limited and should only be exercised if updated data in an ESOO or ESOO Update shows the reliability standard or interim reliability measure is no longer breached and if AEMO considers that it will not reappear before T.

2.3.4

We do not support providing the AER with additional powers

DRAFT RECOMMENDATION 4: MAINTAIN THE AER'S EXISTING ROLE

Maintaining the AER's existing role in assessing reliability instrument gap requests ensures a clear differentiation in roles of market bodies.

Five submissions argued to expand AER powers under clause 4A.C.11 of the NER to reassess or reject a reliability instrument request or retrospectively cancel one or require external auditing of an ESOO results.²⁵ This reflected concern that, while the 2022 ESOO Update released in February 2023 no longer forecast the SA T-1 reliability gap above the IRM, the reliability instrument remained, leading to higher costs being passed onto consumers.

In contrast, the AER argued that providing it with greater powers would undermine confidence in AEMO's ability to forecast gaps through an ESOO and increase uncertainty in the market over respective market body roles and responsibilities.²⁶

The Commission considers that giving the AER new forecasting roles would be a major change to market body roles under the NEL and NER. Providing the AER with additional powers would not contribute to the NEO as it could also lead to uncertainty around market operations and the respective roles of different market bodies.

The AEMC considers changes to the reliability gap forecasting methodology made by AEMO in April 2023, changing the NCP reporting arrangements from T-1 to 1 and extending the timeframe for AEMO to make a reliability gap taking into account more contemporary information, will help ensure that the reliability gap requests are made based on more up to date advice and in a timelier manner.

2.4 We are recommending minor reforms to the market liquidity obligation

The Commission sought stakeholder feedback on the MLO and eleven submissions provided comments.²⁷ The Commission is making a draft recommendation to make minor changes to improve how the MLO operates. We note that a longer term review of market liquidity, particularly in South Australia, may be needed.

2.4.1 Minor reforms could improve the operation of the MLO

DRAFT RECOMMENDATION 5: AMEND THE MLO TO A 10 PER CENT THRESHOLD FOR MLO GROUPS

Changing the threshold from 15 per cent to 10 per cent will ensure that the MLO continues to

²⁵ Submissions to the consultation paper: AEC, AFMA, AGL, DE and EUAA.

²⁶ Submission to consultation paper: AER, p.2.

²⁷ Submissions to the consultation paper: AEC, AFMA, AGL, DE, EnergyAustralia, Engie, EUAA, Origin, SEA Gas, Shell, Stanwell.

support market liquidity in South Australia.

There has been strong compliance by market generators with the six T-3 MLO windows. However, outside of these specific windows, publicly available data through ASX Energy shows that overall market liquidity in SA continues to decline against a number of metrics while remaining broadly stable in other NEM regions.

The ASX has indicated that the MLO also supports price discovery in SA, through establishing transparent prices of what sellers are willing to accept, and what buyers are willing to pay during the MLO windows – which assists with market discovery outside of the windows. This would otherwise not be available in SA with most trades over the counter (OTC).

Submissions put forward a number of proposals to modify the MLO.

EnergyAustralia argued: ²⁸

The bid-offer spread requirements in the Market Liquidity Obligation under clause 4A.G.18(h). In the recent highly volatile market, we expect the spread requirement (e.g. 5% for baseload products in most jurisdictions) has resulted in affected participants being forced to accumulate significant loss-making positions. In other situations, trading exchanges might absorb such losses or provide compensation where market-making is required. For entities to apply to the AER for temporary relaxation or exemption from minimum price spread requirements, for example during abnormal trading conditions, or have spreads adjust dynamically in line with trailing average price observations.

SEA Gas argued: ²⁹

All MLO products, regardless of by whom they are provided, should be required to demonstrate the supply chains in place to ensure physical, versus financial, cover is provided. In turn, this should be reflected in a specific firmness factor for each MLO product offered based on its merits.

Stanwell argued: ³⁰

The threshold be adjusted to target four MLO generators per region, requiring at least two active providers. If a static minimum threshold (such as 15 per cent) means that less than two MLO providers exist in a region the MLO should not be triggered as the cashflow risk imposed on the single MLO generator is likely to be significant and detrimental.

The Commission agrees that minor changes could be made to improve the operation of the MLO in the short term.

²⁸ EnergyAustralia, Submission to Review of the operation of the Retailer Reliability Obligation - Consultation Paper, p.4.

²⁹ SEA Gas, Submission to Review of the operation of the Retailer Reliability Obligation - Consultation Paper, p.2.

³⁰ Stanwell, Submission to Review of the operation of the Retailer Reliability Obligation - Consultation Paper, p.2.

The MLO ends when a region falls below two generator portfolios, for example due to changes in generator ownership or closure of schedule generators. The Commission considers a change to a 10 per cent threshold for MLO groups, with the aim of keeping two generation portfolios under the MLO in each NEM region, would ensure the MLO continues to address market liquidity gaps and support price discovery in SA and other regions which may experience poorer market liquidity. The existing arrangements for the Tasmanian region would be maintained.

The Commission considers that such a change would contribute to the NEO by improving price transparency in the SA region through improved market liquidity, which in turn may help lower costs to consumers.

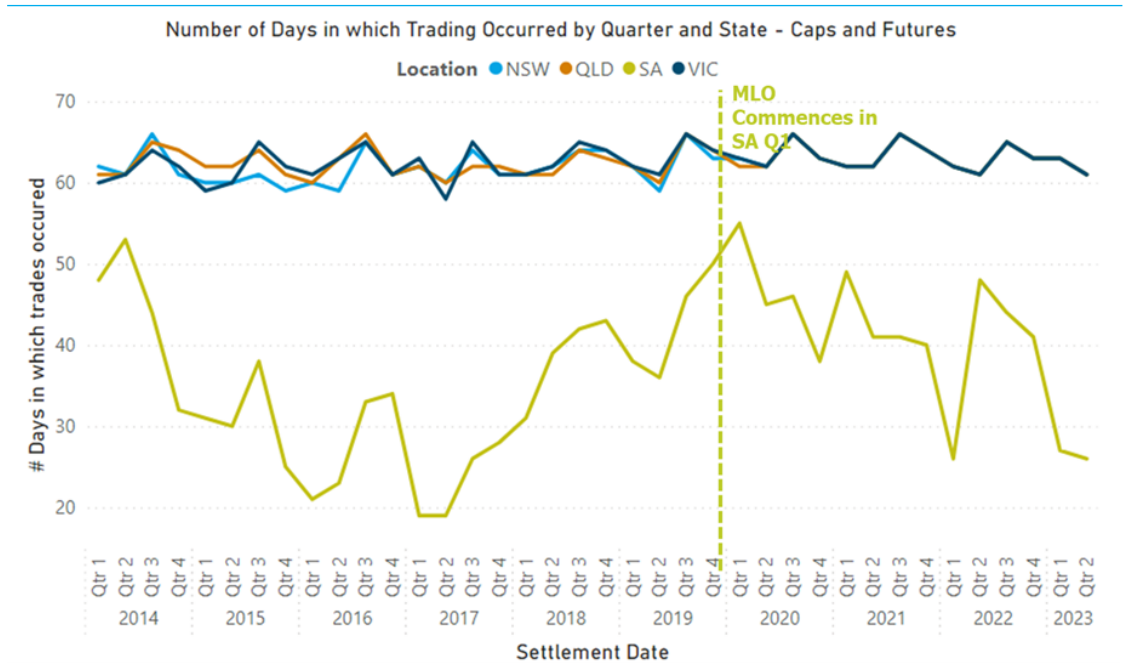
The Commission agrees that the MLO should exclude planned closures from capacity calculations, which occur part way through an MLO period, and that these generators will not be available to deliver firmed capacity during a gap period. This is currently reflected in the RRO rules.

The Commission does not agree to amend the MLO to include seasonal capacity in capacity calculations as seasonal capacity is not part of the data set registered with AEMO.

The Commission has also carefully considered market liquidity in relation to specific reliability instruments.

Figure 2.4 shows that, despite the SA T-3 being triggered annually since 2020 for January to February/March, SA continues to experience significantly fewer days in which trades of caps and futures occur compared with other regions. For SA, this is sometimes less two-thirds than other mainland regions per quarter. There is also significant variation in the number of days per quarter in which trades occurred in SA (ranging between 20 to 55 days per quarter) compared with other regions which typically trade each day that the ASX is open (61 to 66 days per quarter).

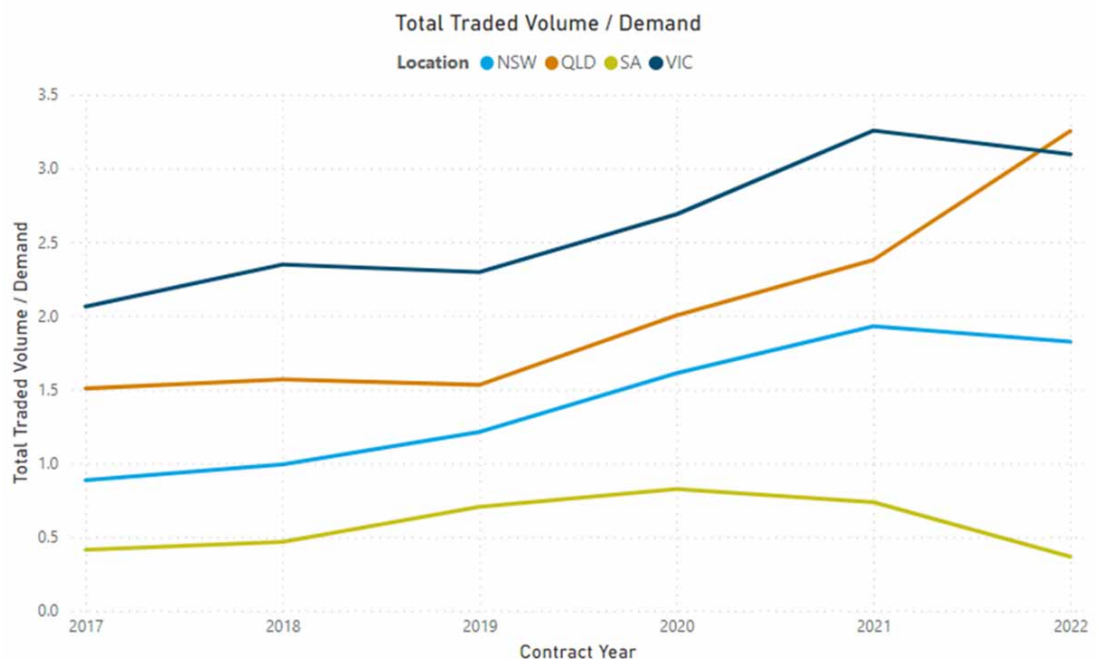
Figure 2.4: Number of days in which trading occurred by quarter and region - caps and futures



Source: ASX Energy data

Figure 2.5 shows that the gap between SA and other states in terms of total traded volumes of caps and futures as a proportion of total demand has continued to widen between 2019 and 2023. Traded volumes in NSW, Queensland and Victoria have risen to 2.5 to 4.5 times total demand between 2019 and 2023, whereas traded volumes in SA have fallen from around 1 to less than 0.5 times total demand in 2023.

Figure 2.5: Total traded volume by demand



Source: ASX Energy data

2.4.2

A longer term review of market liquidity in South Australia may be needed

Three submissions argued that alternative market making arrangements, such as the ASX voluntary market making scheme for exchange-traded electricity futures contracts, could be put in place to support market liquidity in SA outside of the specific MLO windows.³¹

ENGIE argued:³²

The Commission give further consideration to whether the MLO is of value in its own right, and if so, recognise the impost that MLO obligations place on generators and determine a method to remunerate MLO generators that voluntarily offer market liquidity for potential reliability gap periods, or as an ongoing service.

AFMA argued:³³

[W]e think there may be merit in targeted policy measures to increase financial market liquidity by supporting market making. AFMA considers that policy makers could look to build on the ASX's current incentives for voluntary electricity market makers by adopting something like either;

³¹ Submissions to the consultation paper: AFMA, Engie and Origin

³² Submission to the consultation paper: ENGIE, p.2.

³³ Submission to the consultation paper: AFMA, p.3.

- the Singapore Energy Market Authority's Futures Incentive Scheme, which supports market makers on the Singapore Exchange
- the NZ Electricity Authority's hybrid approach of supporting both regulated and commercial market making.

Origin argued:³⁴

The voluntary market maker arrangements of the ASX provide a better mechanism for support liquidity than the Market Liquidity Obligation.

The Commission agrees that further consideration of broader market liquidity in SA as part of a separate review may contribute to the NEO by supporting efficient price outcomes. The Commission may consider, a subsequent self-initiated review into market liquidity including whether mechanisms such as the CIS have improved liquidity and/or alternate arrangements could be put in place to improve market liquidity and reduce costs.

2.5

We are recommending the removal of the voluntary book build mechanism

DRAFT RECOMMENDATION 6: REMOVE THE VOLUNTARY BOOK BUILD MECHANISM

The mechanism is not being used, and removing it would simplify the NEL and NER.

The Commission sought stakeholder feedback on whether process for the voluntary book build mechanism should be amended or if we should consider removing it.

The Voluntary Book Build Mechanism was designed to provide a service for prospective sellers of eligible contracts to have offers of those contracts listed on the Voluntary Book Build site, and for prospective buyers to notify AEMO of their interest in a listed offer. Interested parties are required to pay fees to AEMO for accreditation in the Voluntary Book Build. Of the six stakeholders who commented on the issue, all argued to remove it.³⁵ AEMO did not raise objections to removing the mechanism.

The Voluntary Book-Build Mechanism is not connected with the obligations of MLO generators to offer MLO products. Therefore, any qualifying contracts offered through the Voluntary Book Build do not count towards meeting those obligations. AEMO published two Voluntary Book Build Mechanism instruments in 2020 for South Australia and no offers were made. AEMO has not published any Voluntary Book Build instruments since.

Given that the Voluntary Book Build Mechanism is not being used and there is support amongst submissions for its removal, the Commission agrees that removing the Voluntary

³⁴ Submission to the consultation paper: Origin Energy, p.6.

³⁵ Submissions to the consultation paper: AEC, AFMA, Delta Electricity, Engie, EUAA, Stanwell.

Book Build Mechanism contributes to the NEO by promoting the efficient operation of the NEM by simplifying the NEL and the NER.

This draft recommendation would require amendments to the NER.

2.6 We are making recommendations to change qualifying contract arrangements

The Commission sought stakeholder feedback on whether changes needed to be made to qualifying contracts. Following stakeholder feedback, we are making four recommendations to modify qualify contracts:

1. The AER review expanding eligible demand-side management contract types to increase the pool of eligible contracts and reduce cost and regulatory burden for liable entities³⁶
2. AEMO review expanding the timeframes for the AEMO demand portal being open to expand the pool of eligible demand response contracts and reduce costs
3. The AER review the Contracts and Firmness Guidelines to expand eligibility of qualifying contracts with a firmness of 1 to include caps above five per cent the Market Price Cap to increase the pool of eligible contracts and reduce costs³⁷
4. The AER review opportunities to simplify bespoke methodology and audit arrangements through its guidelines, taking into account the experience of liable entities with the SA T-1 event, to reduce costs for compliance.³⁸

2.6.1 Stakeholders called for changes to qualifying contract arrangements

Qualifying contract arrangements are defined in the NEL, NER and guidelines. Section 140 of the NEL defines qualifying contracts and clause 4A.E.1 of the NER provides details on how the AER will determine qualifying contract arrangements through 'Contract and Firmness Guidelines'.

The AER Contract and Firmness Guidelines set out the contract firmness methodology, the treatment of non-qualifying contracts, the approval process for non-standard qualifying contracts, the establishment and maintenance of an Auditors Panel, the submission of NCP reports and certain information requirements of liable entities.

The NER requires that the AER must have regard to the principle that the contract or other arrangements should support (directly or indirectly) investment in plant or other arrangements that can supply energy that may be dispatched; or can reduce demand for energy that may be activated.³⁹

Section 140 of the NEL establishes the meaning of qualifying contracts as:

³⁶ Refer to AER's Contracts and Firmness Guidelines, found [here](#).

³⁷ Ibid.

³⁸ Ibid.

³⁹ Clause 4A.E.1(b).

1. A qualifying contract of a liable entity is a contract or other arrangement to which the liable entity is a party —
 - a. that —
 - i. is directly related to the purchase or sale, or price for the purchase or sale, of electricity from the wholesale exchange during a stated period; and
 - ii. the liable entity entered into to manage its exposure in relation to the volatility of the spot price; or
 - b. of another type prescribed by the Rules to be a qualifying contract.
2. However, a qualifying contract does not include a contract or arrangement mentioned in subsection (1)(a) that is prescribed by the Rules to be an excluded contract for the reliability obligations

Eight submissions argued for changes to the definitions of qualifying contracts.⁴⁰

Four main suggestions were put forward in submissions to expand the pool of qualifying contracts with higher firmness factors and reduce costs of compliance for liable entities and consumers. The Commission agrees that expanding eligible contract types, could enable more types of firmed contracts to be used to comply with the gap, potentially reducing costs for compliance. Further detail on these recommendations is outlined below.

2.6.2

Expanding the demand side arrangements will better meet the intent of the RRO Policy

DRAFT RECOMMENDATION 7: THE AER REVIEW EXPANDING ELIGIBLE DEMAND-SIDE MANAGEMENT CONTRACT TYPES

This is likely to increase the pool of eligible contracts, to reduce cost and regulatory burden for liable entities.

DRAFT RECOMMENDATION 8: AEMO CONSULT ON EXPANDING TIMEFRAMES FOR THE DEMAND PORTAL BEING OPEN

This will expand the pool of eligible demand response contracts and reduce costs.

Under the NER, qualifying contracts include contracts or other arrangements to support investments that can reduce demand for energy (clause 4A.E.1.(b) of the NER). However, clause 4.A.E.1. of the NER restricts demand response contracts to only be a qualifying contract if it meets the requirements of section 14O(1)(a) of the NEL and is registered in AEMO's Demand Side Participation Information Portal.

⁴⁰ Submissions to the consultation paper: AEC, AFMA, ENGIE, EnergyAustralia, EUAA, Origin Energy, SA Water and Shell Energy.)

This definition in the NER limits types of demand response contracts and the time they can be registered, as the AEMO Portal typically only opens in April. This means that a demand response contract for a gap identified in an August ESOO for a January-March period cannot be registered.

The Commission agrees that two reforms raised in submissions could support greater demand response participation as eligible contracts which would contribute to the NEO by promoting efficient investment to meet the RRO.

Firstly, as outlined in EUAA's submission, AEMO's Demand Side Participation Information Portal could be opened more often to ensure that demand-side contracts can be registered at more times.⁴¹ This change and the change in NCP date would provide longer windows for liable entities to register contracts. This may require AEMO to review its procedures and guidelines.

Secondly, as outlined in SA Water's submission, other types of eligible demand-side management contracts, which do not need to be registered with the portal, could be included.⁴² This would need to be carefully considered so as not to add an additional level of complexity to the assessment by the AER and to protect against double counting.

Options to expand eligible demand-side management types may require amendments to the NER, subject to the AER review.

2.6.3

Increasing the pool of qualifying contracts with a firmness factor of

DRAFT RECOMMENDATION 9: THE AER REVIEW THE CONTRACTS AND FIRMNESS GUIDELINES TO EXPAND ELIGIBLE QUALIFYING CONTRACTS

The AER should review the guidelines to expand the eligibility of qualifying contracts with a firmness of 1 to include caps above 5% of the Market Price Cap to increase the pool of eligible contracts and reduce costs.

The AER's Contracts and Firmness Guidelines provide guidance on firmness ratings for qualifying contracts. The Guidelines outline the extent to which a liable entity's qualifying contracts reduce or increase its exposure to the volatility of the spot price.

All qualifying contracts are allocated a firmness factor between zero and one for each trading interval in the gap period. A higher firmness factor corresponds to lower exposure for the buyer to the volatility of the spot price. Figure 2.6 indicates the firmness ratings for different contract types.

⁴¹ Submission to the consultation paper: EUAA, pg 3.

⁴² Submission to the consultation paper: SA Water

Figure 2.6: Summary of default firmness methodologies for standard qualifying contracts

STANDARD CONTRACT	DESCRIPTION	DEFAULT FIRMNESS FACTOR
Swaps and futures	Applies to swaps and futures with a fixed price and known volume (including a shaped volume) where no other contract limitations are present.	1
Caps with a strike price $\leq 5\%$ of MPC	Applies to caps with a strike price $\leq 5\%$ of MPC where no other contract limitations are present	1
Caps with a strike price $> 5\%$ of MPC	Applies to caps with a strike price $> 5\%$ of MPC where no other contract limitations are present	$\left(\frac{1}{0.952}\right) \times \left(1 - \frac{\text{strike price}}{\text{MPC}}\right)^2$
100 per cent load following contracts (bought)	A load following contract has a fixed price and a variable volume. The buyer and seller of the contract agree that the volume exactly matches the buyer's actual load at each trading interval. The buyer of a 100 per cent load following contract has no exposure to spot price volatility. This contract is fully firm unless the contract contains terms which limit the coverage of the swap.	1
Grandfathered contracts	Grandfathered contracts must meet the definition of grandfathered arrangements in rule 11.116.8. They only apply for large energy users who are either market customers or opt-in customers.	1
MLO products	MLO parties are required to post minimum volumes of buy and sell offers, with a maximum price spread, for standard exchange-traded products in the relevant region for the gap period. These contracts are considered firm under the AER's contracts and firmness guidelines.	1

Source: AEMC

Three submissions argued for the threshold for caps with a firmness factor of 1 be increased from $\leq 5\%$ of the MPC to $\leq 10\%$.⁴³

Shell Energy argued:⁴⁴

There are increasingly cap contracts with a range of strike prices that can be traded on markets like the FEX, rather than the conventional strike price of \$300/MWh. ... We consider that applying a firmness rating of 1 to cap contracts with a strike price of up to 10 per cent of the MPC would still adequately incentivise contracting to manage price volatility while opening up a wider variety of contract markets and therefore lowering costs of consumers.

Other stakeholders expressed concerns that expanding these contract types may lead to higher cost contracts being used, increasing total consumer costs.

The Commission recognises that there needs to be a balance in ensuring that firmed contracts are used to comply with obligations under the RRO and these firmed contracts are not excessively priced.

The Commission recommends the AER review the contracts and firmness guidelines to consider expanding eligibility of qualifying contracts with a firmness of 1 to include caps above five per cent of the MPC. The Commission considers the change may be more likely to increase the pool of eligible contracts and therefore reduce costs.

⁴³ Submissions to the consultation paper: AEC, AFMA and Shell Energy.

⁴⁴ Submission to the consultation paper: Shell Energy, p.4.

2.6.4

Simplifying arrangements for bespoke methodologies

DRAFT RECOMMENDATION 10: THE AER REVIEW OPPORTUNITIES TO SIMPLIFY BESPOKE METHODOLOGY AND AUDIT ARRANGEMENTS

This could be done through reviewing the AER guidelines, taking into account the experience of liable entities with the SA T-1 event, to reduce costs for compliance.

Clause 4A.E.4(b) of the NER stipulates that a bespoke firmness methodology may be applied for a non-standard qualifying contract.

Submissions argued the process for making a bespoke methodology application is too complex. These applications include arrangements for power purchase agreements (PPAs) and load following hedges.

Expanding eligible contract types, for example to demand response contracts, will expand the pool of eligible qualifying contracts. Simplifying the bespoke methods may also increase contract types and reduce costs.

ENGIE and Stanwell argued for changes to simplify guidelines for bespoke methodologies to reduce costs.

Stanwell argued it was:⁴⁵

concerned around the potential costs and short timeframes associated with such an independent audit of its bespoke firmness methodologies.

The Commission agrees that increasing the types of standard qualifying contract types will reduce the need for audits. Continuing to improve audit arrangements will also assist in reducing overall compliance costs and enabling more innovative products to be used for compliance. However, any changes to simplify arrangements need to be balanced against the importance of ensuring that contracts are firm.

Bespoke methodologies and audit arrangements are set out in AER Contract and Firmness Guidelines. The Commission recommends the AER review further opportunities to simplify bespoke methodology and audit arrangements through its guidelines following the SA T-1 gap period.

Any final changes must contribute to the NEO by ensuring efficient investment in firmed capacity.

2.7

We are not recommending changes to liability entity definitions

The Commission sought stakeholder feedback on the thresholds to liable entities and the timing of advice on any exposure during a gap period. The Commission does not recommend

⁴⁵ Stanwell, Submission to Review of the operation of the Retailer Reliability Obligation - Consultation Paper, p.4.

at this stage changes to the definitions of market customers as liable entities, but is seeking further information from stakeholders as part of consultations on the draft report.

2.7.1 Stakeholder views on changes to liable entity arrangements were mixed

Four submissions commented on changes to the thresholds for liable entities or changes to when liable entities are informed of their PoLR costs.⁴⁶

Delta Electricity raised the prospect of a small liable entity being disproportionately impacted if its load changes to below 10GWh. This could happen, for example, due to the loss of a large customer.

EUAA argued that the role of market customers should be reviewed and that there should be a process of providing earlier advice on the exposure of all liable entities during a gap period:⁴⁷ Stanwell also argued for early or progressive advice in advance of having to commit to a compliance position.⁴⁸

2.7.2 Liable entity arrangements remain broadly appropriate.

DRAFT RECOMMENDATION 11: MAINTAIN THE TIMEFRAMES FOR ADVICE ON POLR COSTS

Progressing with the Commission recommendation to change the NCP date from T-1 to T will simplify compliance.

DRAFT RECOMMENDATION 12: MAINTAIN THE EXISTING ROLE OF MARKET CUSTOMERS AS LIABLE ENTITIES.

The Commission considers that liable entity arrangements remain broadly appropriate. Changes to liable entity definitions may be complex to implement and deliver marginal benefits compared to the change to the NCP date from T-1 to T which will simplify compliance arrangements and ensure that ex-post costs are advised as soon as possible post a 50 PoE event.

The Commission does not recommend at this stage changes to the definitions of market customers as liable entities, but is seeking further information from stakeholders as part of consultations on the draft report.

⁴⁶ Submissions to the consultation paper: Delta Electricity, EUAA, Stanwell and Origin.

⁴⁷ Submission to the consultation paper: EUAA, p.3 and 4.

⁴⁸ Submission to the consultation paper: Stanwell, pg 3.

2.8 The Commission will consider changes to opt-in arrangements after receiving feedback

DRAFT RECOMMENDATION 13: MAINTAIN THE EXISTING OPT-IN MECHANISM ARRANGEMENTS.

Arrangements for a non-liable person to opt-in to reliability obligations under the RRO are in section 14E of the NEL and clause 4A.D.2 of the NER. They are designed to enable market customers to opt-in to liabilities rather than through retailers. To date, there have been no opt-in customers in relation to any RRO instruments.

Three submissions commented on opt-in arrangements.

- AEC did not see any need to make changes to the opt-in mechanism.⁴⁹
- Origin argued that three options could improve the opt-in arrangements:⁵⁰
 - A reduction in the maximum penalties that could apply to opt-in customers
 - Opt-in mechanism be repurposed to allow customers to register contracts with the AER which would contribute to the NCP of their retailer
 - Allowing customers to provide an audited demand forecast along with the NCP, and use the forecast rather than actual demand
- SA Water argued that customers should be able to opt-in on an ongoing basis, rather than for each occurrence of a reliability instrument, and that the AER should publish criteria around which opt-in customers are to be assessed.⁵¹

Changing the NCP date from T-1 to T will reduce the cost of compliance by allowing liable entities to report on actual energy use rather than forecast use. These changes should also be reflected in opt-in arrangements.

The Commission does not agree that changes should be made to allow third-party hedging agreements held by customers to be included in a retailer's NCP. Repurposing the opt-in would add new complexities to definitions. The Commission further does not agree that customers should be able to opt in on an ongoing basis. As each reliability instrument is unique (with different liable entities), opt-in applications should be limited to each instance of a reliability instrument and not ongoing.

The Commission does not recommend changes to civil penalty arrangements for opt in customers.

⁴⁹ AEC, Submission to Review of the operation of the Retailer Reliability Obligation - Consultation Paper, p.3.

⁵⁰ Origin, Submission to Review of the operation of the Retailer Reliability Obligation - Consultation Paper, p.5.

⁵¹ Origin, Submission to Review of the operation of the Retailer Reliability Obligation - Consultation Paper, p.3.

2.9 We are recommending that the AER review options to simplify compliance

The Commission sought stakeholder feedback on the compliance process.

Compliance arrangements for the RRO are set out under Part 2A of the NEL. Section 18ZI of the NEL requires the AER to make Reliability Compliance Procedures and Guidelines. The Guidelines include guidance:

- for regulated entities about compliance with the reliability obligations under Part 2A of the NEL;
- for regulated entities about the policies, systems and procedures that they must establish and observe to monitor their own compliance with the RRO;
- on the information and data liable entities are required to provide to the AER about compliance; and
- on carrying out compliance audits, including the costs payable by regulated entities for an audit carried out by or on behalf of the AER.

Six submissions commented on changes to the RRO compliance processes.⁵²

- Delta Electricity noted that significant resources and costs were associated with compliance with the SA T-1 trigger⁵³
- EnergyAustralia argued that the NER should be changed to enable groups with several licenced retail entities to *'be able to be assessed at a group level and for positions to be aggregated'*⁵⁴
- AFMA argued retailers should be able to nominate other entities within the group whose hedge positions could be considered for their RRO compliance⁵⁵
- Origin Energy argued to expand the type of projects to be included in a liable entity NCP to take into account new developments which reach commercial operation past the T-1 cut-off date, but in time to cover the reliability gap period.⁵⁶

2.9.1 The AER has released detailed guidance on compliance arrangements

DRAFT RECOMMENDATION 14: THE AER TO REVIEW OPTIONS TO SIMPLIFY COMPLIANCE ARRANGEMENTS THROUGH GUIDELINES.

In June 2023, the AER released detailed final guidance on compliance arrangements following extensive consultation, including the final Reliability Compliance Procedures and Guidelines.⁵⁷ Given that the AER has only recently released final compliance guidelines, the

⁵² Submissions to the consultation paper: AEC, AFMA, Delta Electricity, EnergyAustralia, Origin and Stanwell

⁵³ Submission to the consultation paper: Delta Electricity, p.2.

⁵⁴ Submission to the consultation paper: EnergyAustralia p.4.

⁵⁵ Submission to the consultation paper: AFMA, p.4.

⁵⁶ Submission to the consultation paper: Origin Energy, p.4.

⁵⁷ AER, Reliability Compliance Procedures and Guidelines - Final Decision, June 2023, found [here](#).

Commission does not recommend major changes to compliance arrangements in the draft report.

The Commission recommends the AER continue to consult with stakeholders on improving compliance arrangements.

The Commission does not recommend assessment at a group level as it could involve complex changes to the liable entity definition in the NEL. Changing the NCP date would instead provide many of the benefits and enable a longer timeframe for the negotiation of contracts within groups.

3 THE DRAFT RECOMMENDATIONS WOULD CONTRIBUTE TO THE ENERGY OBJECTIVES

In conducting reviews, the Commission must have regard to the relevant energy objectives.⁵⁸ For this review, the relevant energy objective is the NEO:

to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to:

1. price, quality, safety, reliability and security of supply of electricity;
2. the reliability, safety and security of the national electricity system; and
3. the achievement of targets set by a participating jurisdiction
 - for reducing Australia's greenhouse gas emissions; or
 - that are likely to contribute to reducing Australia's greenhouse gas emissions.

3.1 How we have applied the NEO to our recommendations

To determine whether any policy recommendations identified in this review promote the NEO, the Commission has used the following assessment criteria:

1. **Operational efficiency:** The regulatory framework should encourage innovation and efficient investment in the supply of energy services.
2. **Appropriate allocation of risk:** Risks should be borne by parties who are best placed to manage them and have the incentives to do so.
3. **Incentives:** The framework should allow the operation of the RRO to effectively facilitate investment in dispatchable capacity and demand response.
4. **Predictability and stability:** The framework should promote confidence in the market by clearly defining roles and responsibilities and ensuring parties have sufficient information to make decisions. It should result in predictable outcomes for participants.
5. **Simplicity and transparency:** The framework should be as simple and practical as possible, avoiding excessive regulation that imposes unnecessary complexity, risks or costs.
6. **Timing and practicality:** Any recommendations should take into account the practicality of developing and implementing proposed changes, as well as whether the recommendations achieve the intended benefits in a timely, proportionate, and targeted way.

3.2 The draft recommendations contribute to the NEO

Having regard to the issues raised in the ToR, the Commission is satisfied that the draft recommendations will, or are likely to, contribute to the achievement of the NEO. The draft recommendations are consistent with the proposed assessment framework:

⁵⁸ NEL s 32.

- **Operational Efficiency:** The draft recommendations will reduce the regulatory burden for liable entities complying with the T-1 reliability instrument through reviews to streamline guidelines and remove unnecessary auditing requirements if a reliability gap is closed between T-1 and T. The draft recommendations also reduce the likelihood of over-contracting by bringing the NCP reporting date to the demand period, which should lower costs for consumers.
- **Incentives:** The draft recommendations will more effectively facilitate investment in dispatchable capacity and demand response by changing the NCP date to T and enabling new investments registered between T-1 and T to be more easily accounted for in NCP reporting by liable entities.
- **Appropriate allocation of risk:** Maintaining key definitions including the definitions of liable entities and MLO groups will ensure that risks continue to be borne by entities who are best placed to contract to support firmed generation.
- **Predictability and stability:** The draft recommendations provide predictability by maintaining key definitions including liable entity arrangements, T-1 and T-3 events, reliability gap forecasts and the MLO, while removing additional regulatory burden and unused elements including the voluntary book build mechanism.
- **Simplicity and transparency:** The RRO at T-3 is understood by market participants. The operation of the RRO at T-1 is new with the draft recommendations designed to simplify its operation by modifying some elements at T-1 including reviews of qualifying contracts, changes to NCP dates and changing time frames for AEMO to request a reliability instrument.
- **Timing and practicality:** The draft recommendations require changes to the NER as well as reviews of guidelines. Some changes may require changes to the NEL, with the aim of reducing regulatory burden for compliance and delivering more practical compliance options including greater access to demand side management.

3.3 The new energy objective will apply to any subsequent reforms

In May 2023, Energy Ministers approved amendments to the energy laws to implement their previous decision to incorporate an emissions reduction component into the NEO, National Energy Retail Objective and the National Gas Objective.⁵⁹

The amendments were passed by the South Australian Parliament on 12 September 2023 and came into effect on 21 September 2023.⁶⁰

In developing these draft recommendations, the Commission has been guided by the NEO as it applied prior to the recent amendments⁶¹. However, the Commission considers the draft recommendations will remain appropriate in light of the changes to the NEO. This is because

⁵⁹ Department of Climate Change, Energy and Environment and Water, Energy and climate change ministerial council meeting communique, 19 May 2023.

⁶⁰ The Statutes Amendment (National Energy Laws) (Emissions Reduction Objectives) Act 2023.

⁶¹ The NEO as in force immediately before the recent amendments was: to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to: price, quality, safety, reliability and security of supply of electricity; and the reliability, safety and security of the national electricity system.

the draft recommendations will, if implemented, promote emissions reduction by improving the operation of the RRO to support investment in firmed renewable generation, storage and demand side management as the NEM transitions to net zero and thermal generators progressively retire.

The Commission will have regard to the new NEO when making the final report for this review and any rule change requests stemming from this review would need to be considered with regard to the new NEO.

ABBREVIATIONS AND DEFINED TERMS

ACCC	Australian Competition and Consumer Commission
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
CIS	Capacity Investment Scheme
Commission	See AEMC
ESB	Energy Security Board
GWH	Gigawatt hours
IRM	Interim Reliability Measure
Liabe entity	Meaning given in the NEL and as determined in accordance with clause 4A.D
Market customers	Meaning Given in clause 2.3.4 of the NER
MLO	Market Liquidity Obligation
MW	Megawatts
NEL	National Electricity Law
NEM	National Electricity Market
NEO	National Electricity Objective
NER	National Electricity Rules
NERO	National Energy Retail Objective
NGO	National Gas Objective
NSW	New South Wales
PPA	Power Purchase Agreement
PoLR	Procurer of Last Resort
Qualifying contracts	Meaning given in the NER
Reliability Instrument	Meaning given in the NEL
RERT	Reliability and Emergency Reserve Trader
RRO	Retailer Reliability Obligation
SA	South Australia
T-1 Reliability Instrument	Meaning given in the NEL
T-3 Reliability Instrument	Meaning given in the NEL
VRE	Variable Renewable Energy

A BACKGROUND AND CONTEXT

In making the fourteen draft recommendations, the Commission has considered the background to the development of the RRO and submissions, as well as new information following the release of the consultation paper on the experience of liable entities and market bodies with the SA T-1 compliance processes and market liquidity arrangements.

A.1 The reliability framework in the NEM is designed to deliver reliability that consumers value

The RRO is part of the overall reliability framework in the NEM to support a reliable power system.

A reliable power system has enough capacity (generation, demand response, interconnection and energy storage capacity) to meet consumer needs. To maintain reliability, a power system needs investment in any new capacity needed to meet changing demand patterns and cover retiring generators. No power system can be 100 per cent reliable, as unforeseen events can always occur. Building a system with sufficient capacity to meet all rare events is prohibitively expensive, as it would involve significant over capitalisation in power system assets that would lead to power prices much higher than consumers would be willing to pay.

The reliability standard is a critical part of the NEM's reliability framework, which seeks to balance the trade-off between reliability and the value which customers place on it.

The reliability standard establishes an expected unserved energy (USE) threshold, at which the cost of infrastructure needed to supply consumers is balanced against the value consumers place on reliability. In the NEM, the reliability standard requires sufficient generation and transmission interconnection so that no more than 0.002 per cent of annual electricity demand goes unmet in each region (0.002 per cent USE).

A.2 The RRO encourages investment in dispatchable energy

In 2019, Energy Ministers, on the advice of the ESB, agreed to the RRO to supplement the reliability standard in supporting reliability outcomes in the NEM and 'encourage new investment in dispatchable energy such that the electricity system operates reliably'.⁶²

Specifically, Energy Ministers were concerned that 'the reduction in dispatchable coal and gas generation and the greater penetration of intermittent technologies such as solar and wind generation present risks to the NEM's reliability'.⁶³

The RRO requires liable entities (typically electricity retailers) to demonstrate they have entered sufficient contracts for dispatchable capacity (including demand response) to cover their share of peak demand where it exceeds the 1 in 2 year peak forecast at periods identified as having a potential shortfall, or gap, of supply to meet demand.⁶⁴ This, in turn, is

⁶² Ibid, p.4.

⁶³ Ibid.

⁶⁴ Section 14R of the NEL.

intended to provide market participants with the necessary confidence to invest in firm generation technology or demand side management to support a reliable electricity supply in the NEM. It was intended to be a long-term solution to ensuring reliability at the lowest cost by preparing for and eliminating forecast reliability gaps before they occur.

The RRO builds on existing spot and financial market arrangements to facilitate investment in dispatchable capacity in the NEM. It obliges retailers, on behalf of their customers, to support the reliability of the power system through their contracting and investment in resources.

A.2.1

Overview of the RRO

The RRO commenced on 1 July 2019, with the aim of providing 'stronger incentives for market participants to invest in the right technologies in regions where it is needed, to support reliability in the NEM'.⁶⁵

The RRO operates as an obligation on retailers to engage in forward contracting.

The ESOO includes a reliability forecast identifying any forecast reliability gaps in the coming five years, defined according to the RRO, and an indicative projection of any forecast reliability gaps in the second five years of the forecast. If AEMO identifies a material gap three years and three months out, it will apply to the AER to start the RRO by making a reliability instrument.

Since the RRO was introduced the South Australian Minister for Energy has had the ability to trigger a RRO within South Australia. Since April 2023, all Ministers in NEM regions also have the ability to trigger a T-3 RRO within their respective jurisdictions.

Where a reliability instrument is made, liable entities are on notice to enter into sufficient qualifying contracts to cover their share of a one-in-two year peak demand. An MLO placed on the largest scheduled generator portfolios requires them to make competitively priced contracts available on the exchanges at known times facilitating access by all liable entities or market customers. AEMO can also run a voluntary book build mechanism to help liable entities secure contracts.

If AEMO assesses, and the AER confirms, that the reliability gap remains, one year out (T-1), liable entities must report their contract positions for the reliability gap period to the AER. If actual system peak demand exceeds an expected one-in-two year peak demand, the AER will assess the compliance of liable entities and determine whether their share of load for the reliability gap period was covered by qualifying contracts.

If not already done so, AEMO may commence procurement of emergency reserves at this point through the reliability and emergency reserve trader (RERT) framework to address the remaining gap with costs to be recovered through the procurer of last resort (POLR) cost recovery mechanism. Entities whose required share of load is not covered by qualifying contracts for the specified period will be required to pay a pro-rata portion of the costs expended by AEMO to manage the market during those periods through the POLR and may

⁶⁵ AER, Retailer reliability obligation, available [here](#).

face fines for having insufficient contract as required in the NEL, up to an individual maximum of \$100 million per region.

The RRO is supported by detailed AER guidelines, which provide detail on how the various stages of the RRO operate. Links to the detailed guidelines are provided here:

- [Contracts and Firmness Guidelines](#)
- [Forecasting Best Practice Guidelines](#)
- [Market Liquidity Obligation Guidelines](#)
- [Opt-in Guidelines](#)
- [Reliability Compliance Procedures and Guidelines](#)
- [Reliability Instrument Guidelines](#)

A.2.2

Obligations on entities

The RRO places specific obligations on entities under the NEL and NER.

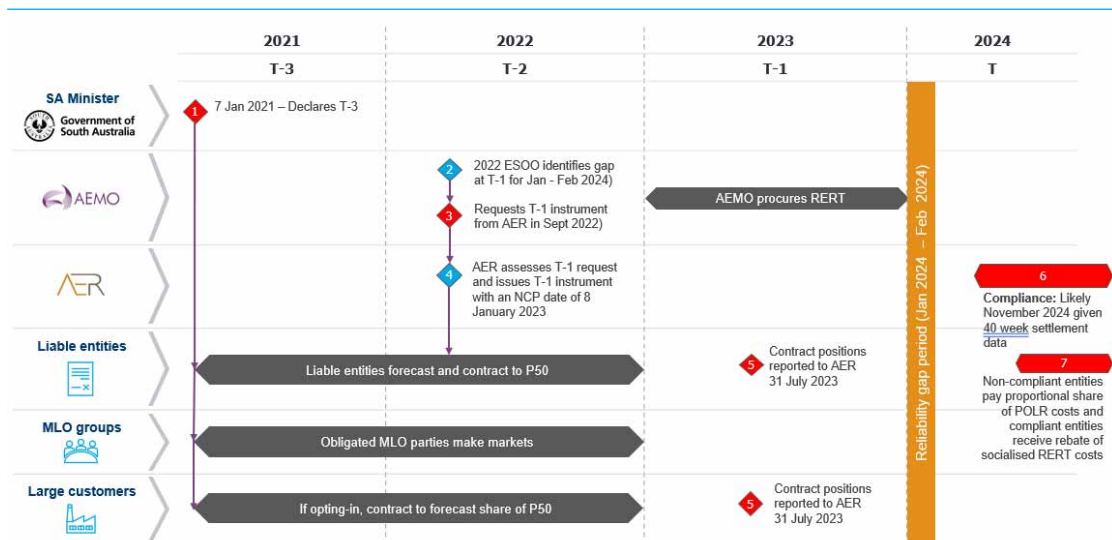
- AEMO's role is to identify forecast reliability gaps in each NEM region in its ESOO forecast, and if a forecast reliability gap arises, also request the AER to issue a reliability instrument.
- The AER's role is to assess and determine:
 - AEMO's forecast reliability gap and trigger the RRO by issuing a reliability instrument
 - Compliance with the MLO following the triggering of the T-3 reliability instrument
 - Liable Entities' reporting and delivery by contract reporting day compliance with the contracts and firmness guidelines following the trigger of the T-1 reliability instrument
 - Liable Entities' compliance with the RRO should a reliability gap period eventuate.
- Liable Entities and MLOs generators and groups must provide certain information to AEMO and AER to meet their obligations under the NEL and NER. When the RRO is triggered, liable entities must enter into sufficient qualifying contracts to meet their share of expected system peak electricity demand reported on a 50 per cent PoE.

AEMO has certain roles in the operation of the RRO outside of advice on T-1 and T-3 triggers under the ESOO, links to these detailed guidelines are provided here:

- [PoLR Cost Procedures](#) (4A.F.10)
- [Reliability Forecast Guidelines](#) (4A.B.4)
- [Voluntary Book Build Mechanism](#)

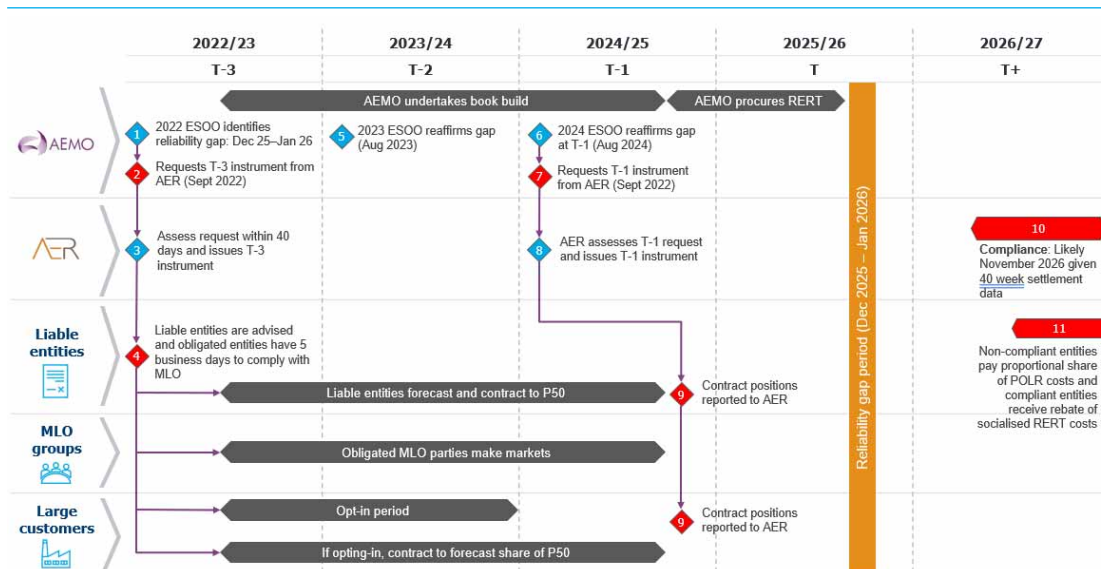
Figure A.1 and Figure A.2 provide further information on the process for establishing and compliance with a Reliability Gap under the RRO in respect of the recent NSW (T-3) and SA (T-1) triggers.

Figure A.1: Example - 2023-24 SA T-1 event



Source: AEMC

Figure A.2: Example - 2025-26 NSW T-3 event



Source: AEMC

A.3

New information is available on the operation of the MLO and SA T-1 trigger

When the consultation paper was released in March 2023, only limited aspects of the RRO had been triggered – the RRO had been triggered on seven occasions. While this provided

some information on the operation of the RRO, the Commission decided to review the RRO over a longer timeframe than required under the NER, with a final report to be released in early 2024. This will ensure that, in its final recommendations, the Commission can consider the longer term experience of the market over the seven trigger events that are either current or have been revoked.

In the consultation paper, the Commission outlined that this longer timeframe will also enable the Commission to consider the following in its final recommendations:

- the form and function of the Commonwealth's Capacity Incentive Scheme
- the AEMC's draft recommendation to extend the application of the IRM to the RRO
- the AER's final Retailer Reliability Obligation Compliance Procedures and Guidelines.

Since the release of the consultation paper, new information has become available to support the Commission's consideration of the operation of the RRO:

- The AER released its final Retailer Reliability Obligation Compliance Procedures and Guidelines in June 2023⁶⁶
- AEMO released its ESOO and Reliability Forecasts Methodology Document in April 2023 which includes 'anticipated' projects in reliability forecasts from the 2023 ESOO⁶⁷
- The SA T-1 NCP reporting dates passed on 31 July 2023 providing new information on compliance experience by liable entities with the SA T-1 event
- The Commission released final rules to extend the IRM to 30 June 2028 to align with the commencement of a potential new form of the reliability standard⁶⁸
- The Ministerial T-3 trigger was extended to all NEM jurisdictions.

The Commission notes that the design and delivery of the Commonwealth's CIS has yet to be finalised, but there have been tenders in NSW and tender arrangements for South Australia and Victoria are expected to be announced in late 2023.⁶⁹

The AEMC has also received information showing compliance with MLO obligations at T-3 events and analysed market liquidity and price changes pre and post reliability gap events.

A.4

Despite the MLO, contract market liquidity in SA continues to be below other regions

The MLO was included in the RRO following reviews by the ACCC and ESB which found SA market liquidity was low:

- **ACCC (2018)** – *'The AEMC should introduce market-making obligations in South Australia... and then review to see if it should be continued, amended or removed in South Australia and, potentially, extended to other NEM regions.'*⁷⁰

66 AER, Reliability Compliance Procedures and Guidelines - Final Decision, June 2023.

67 AEMO, ESOO and Reliability Forecast Methodology Document, April 2023.

68 AEMC, Extension of the application of the IRM to the RRO, Draft rule determination, 13 July 2023.

69 Australian Government Department of Climate Change, Energy, the Environment and Water, Capacity Investment Scheme - Public Consultation Paper, August 2023.

70 ACCC, Retail Electricity Pricing Inquiry—Final Report, June 2018, p.xviii.

- **ESB (2018)** – Recommended the RRO *'as a measure responding to the ACCC recommendation in addressing market power in supply-constrained conditions.'*⁷¹
- **AEMC (2019)** – The AEMC considered a separate rule change request by ENGIE for an alternative market-making arrangement for low liquidity regions (South Australia). The AEMC found that *'market making arrangements additional to the ASX and RRO/MLO schemes are not likely to be efficient.'*⁷²

The Review of the RRO consultation paper sought feedback on the operation of the MLO under the RRO and specifically whether changes should be made to the MLO to improve market liquidity and transparency of contract markets.

A majority of stakeholders did not recommend changes to the MLO and did not indicate that the MLO was creating significant regulatory burden or higher costs.

The AER has indicated that market generators have complied with the MLO requirements at T-3.

The ASX indicated to the AEMC that the MLO plays a useful role in supporting price discovery in markets with low liquidity, which was helpful to market participants.

However, there was broad recognition amongst stakeholders, supported by ASX Energy data, that the MLO in its current form is not making a significant difference to market liquidity in SA outside of the specific reliability instrument windows.

The AEMC has assessed overall market liquidity trends in SA and other NEM regions since the introduction of the MLO using ASX Energy data. This data shows that market liquidity has remained steady across the NEM since the RRO was introduced but has fallen in SA.

ASX Energy data (see Table 5.3.iii.a.) shows that, despite the SA T-3 being triggered annually since 2020 for the January to February/March periods, SA continues to experience significantly fewer days in which trades of caps and futures occur compared with other NEM regions (sometimes two-thirds less). There is also significant variation in the number of days per quarter in which trades occurred in SA (ranging between 20 to 55 days per quarter) compared with other NEM regions which typically trade each day that the ASX is open (61 to 66 days per quarter).

ASX Energy data (see Table 5.3.iii.b.) also shows that the gap between SA and other NEM regions, in terms of total traded volumes of Q1-4 caps and futures as a proportion of total demand, continued to widen between 2019 and 2023. Traded volumes in NSW, QLD and Victoria have risen to 2.5 to 4.5 times total demand between 2019 and 2023, whereas traded volumes in SA have fallen from around 1 to less than 0.5 times total demand in 2023.

Some stakeholders noted that there may be alternative mechanisms to support market liquidity including the ASX voluntary market making scheme for exchange-traded electricity futures contracts.

⁷¹ ESB consultation paper: Market Making Requirements in the NEM, September 2018.

⁷² AEMC, Market making arrangements in the NEM, 19 September 2019, p.iii.

A.5 The SA T-1 event provides evidence of the RRO rules not operating to deliver best outcomes

Many industry stakeholders framed their submissions around the compliance costs and regulatory burden associated with compliance with the SA T-1 trigger event for the period 8 January 2024 – 29 February 2024. These stakeholders argued that a range of overlapping issues around the operation of the RRO under the NER and NEL led to the T-1 SA event being triggered unnecessarily and that this will lead to higher costs for consumers and additional costs which are not able to be reclaimed by market participants.

Ten submissions (AEC, AFMA, AGL, DE, AGL, ENGIE, EnergyAustralia, EUAA, SA Water and Shell) argued to extend AER powers to override a request by AEMO for a T-1 Reliability Instrument. Two submissions (AER and Stanwell) argued that the AER should not have additional powers.

Four of these submissions (AEC, AFMA, AGL and EUAA) further supported improving AEMO's forecasting methodology. Other stakeholders (AEMO, AER, AGL) acknowledged AEMO had released a new 'ESOO and Reliability Forecast Methodology Document – 24 April 2023' during the consultation period for the review, to improve forecasting through including 'anticipated projects' in reliability forecasts.

Industry and representative submissions broadly argued that the way the RRO was applied to trigger the SA T-1 event led to additional and unnecessary costs, borne by consumers, above what was considered needed to meet the IRM. Lower cost opportunities to close gaps were also available to be accessed by liable entities, such as projects registered between T-1 and T but were unable to be sufficiently accessed based on the rules and guidelines.

The timeline for the SA T-1 trigger event and key additional information are presented in Table A.1.

Table A.1: Timeline of SA T-1 trigger events

DATE	EVENT
31 August 2022	The 2022 ES00 released on 31 August 2022 showed a reliability gap (at T) was likely in SA for the period 8 January 2024 and 29 February 2024.
1-14 September 2022	The AER followed the processes required under the NER and consulted with stakeholders on a proposed reliability instrument. Submissions argued that AEMO's methodology for estimating the gap was flawed as it did not consider 'anticipated' projects. AGL raised that 'AEMO has classified both Iberdrola's 123MW Bolivar Power Station and AGL's 250MW Torrens Island Battery as 'anticipated' when both are on track to be operational before the forecast reliability gap period starts in January 2024.' (AGL, 14 September 2022).

DATE	EVENT
24 October 2022	<p>The AER released a Reliability Instrument with a contract position date of 6 January 2023.</p> <p>Clause 4A.C.11 of the NER requires the AER to assess AEMO's methodology only for material errors or incorrect assumptions. However, industry submissions to the review argued that the AER should be given additional powers to reject or over-ride a decision based on new information.</p>
26 October 2022	AEMO commences consultation on a new NEM Reliability Forecasting Guidelines and Methodology Consultation, including proposing that ' <i>anticipated projects should be included in the reliability forecast... after the T-1 year for RRO purposes</i> '.
Early January 2023	Cap contracts for the SA T-1 gap period increased (EUAA, April 2023).
6 January 2023	Net Contract Position (NCP) date: liable entities were required to record their NCP for each trading interval between 5 pm and 9 pm, for each working weekday during the period 8 January to 29 February 2024 inclusive.
8 February 2023	Bolivar Power station registered with AEMO.
16 February 2023	Osborne Power Station closure delayed from December 2023 to December 2026.
21 February 2023	AEMO releases an 'Update to the 2022 ESOO' showing the IRM would not be breached between 8 January to 29 February 2024. This resulted from Bolivar Power Station and Tailem Bend Battery being committed projects and the delayed closure of the Osbourne Power Station.
24 April 2023	AEMO releases its ESOO and Reliability Forecast Methodology Document to include 'anticipated' projects in forecasts from the 2023 ESOO.
9 June 2023	The AER releases its final RRO reliability compliance procedures and guidelines for liable entities.
31 July 2023	NCP reporting date for liable entities (except for new entrants, which is 30 April 2024).
31 August 2023	AEMO releases its 2023 ESOO showing the SA T-1 period reliability gap forecast again breaches the IRM as a result of changes in demand forecasts and generation assumptions.
8 January - 29 February 2024	Reliability gap period.
1 March 2024	Reliability Instrument closes.
November 2024	Compliance date (40 weeks after settlement date) for gaps above 50 PoE.

The Commission agrees that, while the SA T-1 event was applied by the AER and AEMO under the NER and NEL, the way the RRO is operationalised through the NEL, NER and associated guidelines is likely to have led to additional regulatory burden and unnecessary costs for consumers for contracting that may not have been needed to address reliability gap.

Examples of issues that appeared include:

- Market bodies were not able to take into account new generation information prior to establishing the reliability instrument due to the way the T-1 trigger is established under the NER.
- When new advice became available (including new forecasting methodologies) showing the gap may close in the 2022 ESOO Update, the way the T-1 trigger is established under the NER meant market bodies were unable to take this new information into account.
- Liable entities required to contract to close the gap were unable to sufficiently provide evidence of newly built, committed or extended firmed generation up to the T-1 NCP date.
- The NER establishes complex requirements for liable entities. AER guidelines could be updated on an earlier basis to better support auditing arrangements and provided greater certainty over qualifying contract arrangements.

The Commission also notes that forecasting reliability gaps is subject to some uncertainty due to changes in generation and demand. While the 2022 ESOO Update showed that the SA T-1 reliability gap was no longer below the IRM threshold, the 2023 ESOO subsequently re-established the gap as above the IRM.

Costs for a T-1 trigger include administration, contracting and possible PoLR costs.

There are some early indications that the SA T-1 has led to higher costs to consumers. While it is difficult to know with certainty if the increased contracting costs result from the operation of the SA T-1 or specific decisions by retailers, in their submissions to the IRM Review, Shell and EUAA noted changes in contract markets in SA around the NCP date.

EUAA provided evidence in their submission (presented below in Figure A.3) to the review of the IRM of a *'significant rise in Q1, 2024 forward cap prices that occurred subsequent to the AER's decision. It also shows the significant separation from prices in Victoria'*.⁷³

⁷³ EUAA, Submission to Review of the Interim Reliability Measure, 13 April 2023, p.3.

Figure A.3: Victorian and South Australian Cap Prices

	Victoria Cap Price \$/MWh			South Australia Cap Price \$/MWh		
	Peak	Off-peak	Flat	Peak	Off-peak	Flat
1 July	69.00	4.46	31.50	95.00	5.94	43.25
1 August	64.00	4.62	29.50	97.50	7.15	45.00
30 September	72.50	5.38	33.50	121.50	8.77	56.00
1 November	72.00	4.88	33.00	192.50	9.21	86.00
15 November	62.50	7.00	30.25	226.00	20.77	106.75
1 December	65.50	6.98	31.50	233.00	21.31	110.00
3 January	38.50	4.51	18.75	150.00	12.32	70.00
1 February	41.50	4.50	20.00	112.00	7.88	51.50

Source: EUAA, Submission to Review of the Interim Reliability Measure, 13 April 2023, p.3.

While it is likely that the SA T-1 has triggered higher costs, the full costs of the SA T-1 event may not ever be known. Liable entities are required to report their NCP report to the AER by 31 July 2023. The NCP report does not report how much liable entities paid for their contracts and contract settlement may not be known until the contracts end at T and settled (and even then, it will only be the counter-parties that know the full costs). PoLR costs may not be known until after 40 weeks after T (November 2024).