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Reliability Panel
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Dear Panel Members

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AEMC Reliability Panel, Reliability Standard and Settings Review 2018, Issues Paper, 6 June 2017

EnergyAustralia is one of Australia's largest energy companies with over 2.5 million electricity and gas accounts in NSW, Victoria, Queensland, South Australia, and the Australian Capital Territory. We also own and operate a multi-billion dollar energy generation portfolio across Australia, including coal, gas, and wind assets with control of over 4,500MW of generation in the National Electricity Market.

EnergyAustralia appreciates the opportunity to comment on the Reliability Standard and Settings (standard and settings) Review issues paper, noting the significant changes the market is currently undergoing. These changes provide particular challenges in assessing the appropriate standard and settings from 2020 onwards.

We consider that the current standard and settings strike a good match between providing the correct price incentives in the market for new generation, while not creating unmanageable risk of exposure to extreme prices. However, we also note that multiple factors, other than price, are creating large distortions in the appropriate signals that are impeding the effectiveness of the standards and settings to drive investment.

With the level of change being considered in the market at present it would be difficult to confidently assess the impact of changing the standard and settings. In addition to the government interventions in the market, a large suite of Rule changes fundamentally altering the nature of the market are underway. These include changes relating to the system security market frameworks review, adjusting the mechanism of central dispatch, redefining embedded generator performance standards and altering frequency control markets and mechanisms.

Reliability Standard

We note that as part of the review, the reliability standard of 0.02% unserved energy will only be reassessed if there is a likely to be a material benefit in doing so. We do not consider it likely that that the threshold for reassessment has been met at this time, as there have not been significant reliability issues in the market up to this point. We see that the current

standard still provides an appropriate balance between providing a reasonable level of reliability without significantly increasing costs to consumers in providing a higher target.

While this standard has been met consistently in most regions, in those instances where the standard was breached or was close to being breached, there have been government or market operator interventions to procure additional supply. This suggests that there is a desire for a higher level of reliability in some jurisdictions, although the interventions have come at significant costs to consumers. As discussed below, these interventions have also primarily been related to system security issues rather than reliability. Further, these interventions prevent a market based reaction to a tightening of supply that would be expected under the standards and settings.

Given the transitional period the market is undergoing, we consider that changing this standard is unlikely to provide a material benefit. It is likely that stability in regards to this key measure is more beneficial to consumers until such time as the distortionary effects of policy instability are reduced. We also consider that highlighting the potential costs to consumer of embedding a higher reliability standard would be useful in guiding governments and regulators when they seek to intervene to provide a higher level of reliability than set under the standard.

Reliability Settings

As part of the review we understand that both the market price cap (MPC) and cumulative price threshold (CPT) will be reassessed, while the administered price and market floor would only be reassessed if there was likely to be a material benefit in doing so. Similar to the reliability standard we consider that any reassessment needs to factor in that stability is both important for consumer outcomes while also providing an appropriate investment environment. However, we also understand that modelling of the settings will need to take into account the proposed changes to the National Energy Market (NEM) covered in the previously mentioned reviews and Rule change proposals. Factoring in a diverse and transforming energy mix is also necessary to ensure the settings will be appropriate over the period they cover.

In terms of the MPC and CPT we note that multiple directions from AEMO have occurred in the last 12 months. The MPC and CPT are both meant to drive outcomes that allow the reliability standard to be met without such interventions, and it would be useful that reassessment of the MPC and CPT takes into account ongoing and increasing use by AEMO of directions. However, we also see that some of the directions are primarily due to system security concerns and less so due to a lack of generation within specific regions. This includes directions for synchronous generation to run in place of wind, in order to maintain system strength. We consider that such intervention does not necessarily point to the MPC and CPT not functioning as intended.

In regards to the MPC specifically, the Reliability Panel should be seeking to strike the right balance between providing incentives to invest in the market while not having extreme outcomes from exposure to the price cap. The setting of the MPC should also be such that it continues to drive a strong level of participation in financial markets to minimise exposure to the spot price.

Any significant increase has the potential outcome of causing extreme financial stress to retailers that are exposed to the spot price, or generators that are unable to defend hedging positions. A cause of concern would be that if growing volatility is experienced due to the continued penetration of intermittent generation, without corresponding levels of storage,

participants are likely to suffer increased exposure to the price cap as the market transitions. Obviously, this exposure would be exacerbated by a higher MPC setting.

Any reduction in the MPC should be considered against the possibility that it would reduce incentives to invest in adding generation capacity to the market. Combined with government interventions in this sector, such a reduction may impact on the market's ability to respond to market signals and meet the reliability standard.

Similar consideration is also necessary in respect of the CPT. It does appear to us that the relationship between the CPT and MPC acts to allow suitable investment signals while preventing unmanageable long term prices impacting participants and consumers. Assessment of the ratio between the MPC and CPT should take into account the benefit of it remaining as it is, therefore providing a measure of certainty to the market around the pricing outcomes during peak demand times, times of network constraints or supply shortages.

In determining whether the materiality threshold has been met for a reassessment of the administered price, a key issue is whether this price is appropriate given current gas prices and the effect on costs for gas peaking plant. During the transition from the previous high levels of baseload coal generation, there is likely to be a greater reliance on gas powered generation and higher volatility. This may see gas generators exposed to longer periods of administered pricing. Ensuring that the administered price does not lead to adverse outcomes for gas generators, in an already tight market, must be part of this assessment. We do not consider that there is likely to be a material benefit in reassessing the market price floor.

As pointed out in the issues paper, any modelling as part of the reassessment of the MPC and CPT should have a clear approach utilising a range of scenarios that cover both the growing disconnect between reserve, demand and price and the increasing penetration of intermittent energy resources. Modelling the effects of the likely changes to the NEM, and related impacts on financial markets, will require further consultation with stakeholders to ensure a transparent approach is taken. We look forward to engaging with the Reliability Panel on this issue as the review progresses.

If you would like to discuss this submission, please contact me on (03) 8628 1393 or at chris.streets@energyaustralia.com.au.

Regards

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