

Paul Smith
Chief Executive
Australian Energy Market Commission

Online lodgement at www.aemc.gov.au

4 September 2014

Dear Paul,

RE: First Interim Report – OFA Design and Testing (Ref EPR0039)

GDF SUEZ Australian Energy (GDFSAE) welcomes the opportunity to provide comment on the Australian Energy Market Commission (AEMC) First Interim Report on the Optional Firm Access Design and Testing (Interim Report).

GDFSAE has appreciated the opportunity to participate in the AEMC working group which has considered each of the elements which are discussed in the Interim Report. The AEMC and AEMO have been conducting a very extensive and thorough examination of the elements of the OFA model, and have provided opportunities for the working group members to participate.

Overall comments

GDFSAE (previously International Power) has been an advocate of firm transmission access arrangements for many years, and continues to support the concept of Optional Firm Access (OFA). GDFSAE support for firmer access arrangements is to a large extent based the desire to achieve greater certainty for existing and new entrant investors in generation resources, and to provide more effective locational signals.

Some industry participants have observed that the catalyst for change towards firmer network access arrangements has disappeared due to the decline in electricity demand seen in recent years, and forecast to continue in coming years. GDFSAE acknowledges that the lack of demand growth substantially reduces the urgency for change, but believes that it also provides an ideal opportunity to introduce new access arrangements in an environment where participants can become familiar with the new measures before they become critical to their business operation and risk management.

A further point to note is that the on-going introduction of large-scale intermittent generation stresses the network design and creates new transmission constraints and challenges.

GDFSAE is aware that the OFA model as conceived from the Transmission Frameworks Review was regarded by many industry participants as an overly complex proposal, and not commensurate with the issue to be solved. This perception of unnecessary complexity has led some participants to conclude that the costs and risks of the OFA proposal are unlikely to be balanced by the benefits.

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GDFSAE has argued that the complexity is inherent in the NEM hub-and-spoke model, and that any generators that are participating actively in the NEM will need to have trading expertise which understands the nature of network congestion, and the potential costs and risks that arise. The OFA proposals provide new and more effective mechanisms to deal with existing complexity.

Although GDFSAE's view is still that the fundamental complexity is intrinsic to the NEM model, we have observed that as the AEMC design and testing project has considered a number of issues in detail, there have been a number of additional layers of complexity added to the basic model. For example, the TNSP incentive scheme has evolved to include shortfall factors and nested caps, and short term trading arrangements are being introduced.

With these points in mind, GDFSAE is now concerned that despite the excellent work that has been carried out within the Transmission Frameworks Review and more recently, as part of the detailed design and testing project, there is a risk that the industry will reject the proposed OFA model on the grounds of complexity. GDFSAE believes that this risk is being compounded by the fact that the choice being offered to industry is apparently "all or nothing". In other words, the industry is being asked whether it wants to implement the full OFA package, inclusive of all elements, or to do nothing at all.

GDFSAE believes that a better approach would be to identify from the various components of the OFA package, those elements which are likely to provide the most benefit for the least complexity and cost. GDFSAE is of the view that a substantial benefit can be gained by implementing access settlements and simply firming up the access provisions in the planning domain, as this is the timeframe where generator investment decisions are influenced and made.

Firm access standard

The Interim Report notes that the firm access standard has evolved from what was proposed in the Transmission Frameworks Review to include both a planning standard and an operating standard.

GDFSAE supports the separation of the planning and the operating standards into separate requirements, rather than the combined standard that was proposed in the Transmission Frameworks Review. This creates a clearer distinction between the planning functions of the TNSP, and their interaction with the market in the operational domain.

GDFSAE is generally supportive of measures that aim to provide TNSPs with operational incentives to deliver the levels of access that have been agreed. However, it is also recognised that operational outcomes are subject to a number of uncertainties which cannot always be anticipated or managed.

GDFSAE believes that the certainty that a generator seeks is to a large extent, a commitment from the TNSP that it will plan and maintain its network in such a way that it continues to recognise the agreed access levels for the duration of the agreement. Although this would leave operational outcomes subject to some uncertainty, it is expected that if the network planning processes preserve a generator's agreed access level, then the operational outcomes should in most cases, be adequate.

GDFSAE believes that a better approach to implementation of the OFA would be to introduce the planning standard initially, and then at some later point in time, give consideration to whether the additional step of the operational standard is warranted.

The access settlement process which provides the basic mechanism of financial transactions between firm and non-firm generators can still be implemented without the operational firm access standard.

TNSP incentive scheme

The aim of applying incentives on TNSPs' to encourage operational outcomes that take account of market conditions is broadly supported by GDFSAE. The Interim Report sets out a detailed mechanism that could potentially encourage TNSPs' to ensure that they provide transmission capacity to match their access agreements.

The incentive scheme aims to filter out events that are outside the control of the TNSP, whilst continuing to encourage the TNSP to maintain access levels. GDFSAE agrees that a TNSP should not be penalised for events that are outside of their operational control, although we note that a market participant that takes a commercial position and then suffers an unexpected operational outcome, does not normally have an ability to exclude such events from impacting on their commercial position.

Although the intent of the TNSP incentive scheme is desirable and supported by GDFSAE, there is a legitimate question as to whether the complexity that would be introduced is warranted, at least initially.

If the option of introducing the planning standard without the operational standard were to be taken up as suggested in the preceding section, then there would be no need to implement the TNSP operational incentive scheme. GDFSAE suggests that this simplified approach should be considered.

Inter-regional access

The proposals in the Interim Report for inter-regional access would provide a firmer and more certain product than the current SRA product. This is an important aspect of the OFA regime as the current inability for participants to access the price of neighbouring regions with any certainty is an important restriction within the current NEM.

GDFSAE agrees that an auction process is likely to be an efficient and effective method for offering and allocating long-term inter-regional access. However, we suggest that in the interests of focusing initially on the key components of firm access, the initial implementation of OFA should proceed with only the long-term inter-regional access, and the proposed short-term inter-regional access should be left for consideration at a later time.

Short-term firm access

The proposed arrangements for short-term access have some appeal as they would enable a TNSP to offer firm access at a location where there was surplus network capability. One potential benefit of this approach is that it would enable a generator to gain firm access for a short period of time, at relatively low cost, since the short-term access would be based on existing network capability.

Despite the expected low cost of short-term access, GDFSAE is somewhat sceptical of the value that generators will place on short-term access. If a generator values firm access at their particular location, it is more likely that this is something that would be needed by that generator for a longer period of time, to support their physical and commercial arrangements. If this is the case, GDFSAE questions whether the complexity associated with short-term access is warranted.

Similar to previous suggestions, GDFSAE would suggest that the AEMC do not proceed with the short-term access arrangements in their initial implementation of OFA. Short-term access could then be considered at a later review point, in light of experience gained and issues as they stand.

Transitional access

As noted in the Interim Report, the provision of transitional access to existing generators for a substantial period is important to avoid abrupt changes in aggregate levels of agreed access as required by the fourth objective of the transition to optional firm access in the Transmission Frameworks Review.

When businesses made the decision to invest in existing generators in the NEM, they could not have anticipated that they might have to pay an additional amount of money in the future, in order to continue to be able to provide their generation to the regional reference node. It is also likely that at the time of the original sale of generators to private investors in the NEM, the purchase price included some consideration of the costs of providing access to the regional reference node.

The arguments for sculpting back the transitional access are less compelling. One argument for sculpting included in the Interim Report is that existing generators may hold on to access that they do not value, thus creating a barrier to new entrants. However, if a generator comes to the view that they do not require their transitionally allocated firm access, then that generator would have an incentive to gain some payment from another generator that does value the firm access. In this way the efficiency of firm access supply is not impaired.

The Interim Report raises the point that where a generator has been allocated transitional access and the TNSP finds that the network asset that supports the generators access level needs replacing, the TNSP might prefer to replace the network asset with a smaller and less expensive option, particularly when faced with falling demand. GDFSAE suggests that this possible scenario should not be managed by sculpting away transitional access. A better approach would be that if such circumstances were to arise, the TNSP could indicate to the relevant generators what replacement they propose (to continue to meet the reliability requirements), and what the additional cost would be to complete the upgrade to the level needed to maintain the transitional access levels. The generators should then be given the option of contributing to the funding of the additional upgrade.

For the reasons set out above GDFSAE believes that the issues being put forward in support of sculpting can be dealt with through alternative means, and that the transitional access levels therefore do not need to be sculpted away. GDFSAE therefore supports option 2 – no sculpting of initially allocated transitional access, with reliance on secondary trading to achieve an efficient allocation of access.

Staged implementation

GDFSAE supports the temporal staging of the OFA elements. The alternative simultaneous implementation would impose a dramatic single step change onto the market participants and TNSPs, with many different elements interacting in new and uncertain ways. This would impose a great deal of risk and uncertainty for the industry. It is difficult to justify such a dramatic approach given that the drivers for introducing OFA are somewhat attenuated at present due to lower demand growth.

The other alternative implementation option of geographic staging should be rejected by the AEMC as it would be counter to the notion of a national electricity market, and would impose extreme operational difficulty for participants that operate in multiple regions. Single regions should not be given the power to veto the overall OFA implementation.

GDFSAE believes that the temporal staging approach is the better approach as it allows the industry to become familiar with key elements of the OFA package incrementally.

The Interim Report states that there would be no decision points in temporal staging with the incremental implementation timetable established up front. GDFSAE suggests that in response to concerns about unnecessary complexity in elements of the OFA model, the incremental implementation timetable should not be fixed, but that review / decision points be set at appropriate periods into the future to review what has been implemented to date, and to decide whether any additional elements are likely to add sufficient benefit to justify their implementation.

With this approach in mind, GDFSAE believes that the core elements that should be included in the first stage of implementation are access settlement (including transitional access allocation) and secondary

trading. The firm access standard should not be included in this initial stage, with a 'best endeavours' obligation on the TNSPs to support and maintain their networks to ensure delivery of firm access.

As the TNSPs move through their regulatory revenue approval processes, then the firm access planning standard should be applied. GDFSAE believes that the operational standard introduces a lot of complexity for arguably, little benefit, and should therefore be one of the elements subject to a future review/decision point.

Please do not hesitate to contact me if you wish to discuss any aspect of this submission.

Yours sincerely,



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