



1 August 2017

Michael Bradley
Senior Advisor
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Dear Mr Bradley

RE: Non-scheduled generation and load in central dispatch

ERM Power Limited (ERM Power) welcomes the opportunity to respond to the Australian Energy Market Commission's (AEMC) draft determination on non-scheduled generation and load in central dispatch.

About ERM Power

ERM Power is an Australian energy company operating electricity sales, generation and energy solutions businesses. The Company has grown to become the second largest electricity provider to commercial businesses and industrials in Australia by load¹, with operations in every state and the Australian Capital Territory. A growing range of energy solutions products and services are being delivered, including lighting and energy efficiency software and data analytics, to the Company's existing and new customer base. ERM Power also sells electricity in several markets in the United States. The Company operates 497 megawatts of low emission, gas-fired peaking power stations in Western Australia and Queensland. www.ermpower.com.au

General Comments

ERM Power is disappointed with the AEMC's proposal not to make a rule change requiring non-scheduled generation and price responsive load to participate in the central dispatch process. We believe that the Commission has erred in focussing only on past behaviour and ignoring the potential future impacts. We also contend that the rationale behind the draft determination sets a precedent for how the Commission must now treat the Five Minute Settlement rule change.

We consider that by not making the non-scheduled generation rule change, there is greater potential for more non-scheduled generation to enter the market, potentially constraining off lower-cost generators in some instances and distorting the dispatch and pricing process. Rather than dismissing the rule change entirely, ERM Power considers that the AEMC should have required new generation with a nameplate capacity of 5MW or greater to register as scheduled generators. Exceptions could apply for generation used as part of an industrial process that is rarely, if ever, expected to export into the market.

¹ Based on ERM Power analysis of latest published financial information.

Links to Five Minute Settlement

In our submission on the AEMC's Five Minute Settlement Directions Paper, ERM Power flagged the common elements in that rule change and the non-scheduled generation and load in central dispatch rule change. All three rule changes are seeking to improve the dispatch process of the National Energy Market by ensuring that prices more accurately reflect the supply-demand balance for each dispatch interval. Yet, the Commission has treated the Five Minute Settlement rule change separately from ENGIE and Snowy Hydro's respective rule changes on non-scheduled generation and price responsive load. Treating the three issues together as raised on numerous occasions by participants during the AEMC's Five Minute Settlement Rule industry workshops would have allowed for the consideration of the risks and benefits given the inter-related nature of the three rule changes. Doing so would have provided a consistent approach that may have found a single solution that would provide the greatest benefits for the lowest cost. As it stands, this rule change determination significantly alters the risk profile of five minute settlement.

Our submission on Five Minute Settlement also called for the AEMC to reform the thresholds for non-scheduled generation as a precursor to considering the implementation of Five Minute Settlement. This was to remove the inefficient impact of non-scheduled generation opaquely generating into the market post the setting of price and dispatch. With the AEMC rejecting changing the thresholds for non-scheduled generation as part of this rule change, we strongly believe that the AEMC must consider the increased risks attached to Five Minute Settlement.

Primarily, our rationale for changing the thresholds for non-scheduled generation related to the potential for large volumes of battery storage to switch from exporting to the grid, then suddenly switching to importing energy. We note that the Australian Energy Market Operator (AEMO) has provided guidance on battery storage registration through its guide to generator exemptions and classification of generating units. As part of this guide, AEMO will require battery storage facilities of more than 5MW and less than 30MW to be registered as both market generators and loads. Additionally, AEMO tells generators with a battery storage facility less than 30MW that they "should consider applying" to be classified as scheduled units. If the battery storage facility requests classification as a non-scheduled generator and load, then AEMO may impose conditions or require scheduling under clauses 2.2.3(c) and 3.8.2(e) of the National Electricity Rules.

Although this case-by-case approach may partially deal with some of the concerns about large volumes of non-scheduled generation rapidly entering the system it may result in inconsistent registration outcomes. A consistent application of the rules is necessary to provide certainty to both battery storage proponents and other generators who may be impacted. The AEMC could have provided this kind of greater certainty to the market by deciding to make the non-scheduled generation rule change.

In its summary of the draft determination, the AEMC explains that one of the reasons for not making the rule change is:

"To the extent that benefits are uncertain and the costs may be inefficient and flow through to consumer pricing, the proposed changes will not, or are not likely to, contribute to the achievement of the NEO."²

If the AEMC finds that there are uncertain benefits and inefficient costs that will flow through to consumers, it is reasonable not to make a rule change. ERM Power adds that the Five Minute

² AEMC 2017, Non-scheduled generation and load in central dispatch, Rule Determination, 20 June 2017, Sydney, p. vi

Settlement rule change can also be described in these terms. As we and others have argued, the Five Minute Settlement rule change may well have benefits, but these are highly uncertain and could well be overwhelmed by the costs of changing systems, installing new generation technologies and new metering that will be required under Five Minute Settlement. We therefore consider that the AEMC's rationale used in the non-scheduled generation and load in central dispatch rule change must also be applied to the Five Minute Settlement rule change. This is further supported by a further statement in the summary, repeated later in the draft determination that:

"The Commission recognises that many businesses are already under financial pressure from high energy costs, and does not consider it reasonable to add additional costs when the benefits that may accrue ... are uncertain".³

To fail to do so would introduce an inconsistent approach in the manner in which the AEMC considers and determines rule changes to the detriment of the rule change process and the NEM.

Both households and business are concerned by the recent rises in the costs of electricity. ERM Power's data shows commercial and industrial customers are paying up to 170 per cent more for energy and green schemes in the past couple of years. The AEMC is right to consider the potential for a rule change to increase energy costs for businesses as a reason to not make a rule change. Again, we believe that this applies equally to the Five Minute Settlement rule change and have made this clear in our submission to the Directions Paper. It would therefore be inconsistent for the AEMC to reach different conclusions on the two rule changes given the arguments made in this draft determination.

The AEMC also argues that:

"...there is a risk that adding costs to small non-scheduled generators will not only disrupt the business models of existing generators but may also deter new and innovative investment in the sector."⁴

ERM Power strongly supports markets that encourage innovative investment and imposing needless restrictions could hamper the introduction of new solutions. However, the decision to install small, non-scheduled generation may not represent genuine innovation if the rationale for doing so is simply to exploit a loophole in the market rules.

Further, ERM Power and others have argued that the business model of existing generators would be severely disrupted by the change to five minute settlement. It will therefore be incumbent on the AEMC, in its draft determination on the Five Minute Settlement rule change, to weigh the disruption to existing generators against the purported enhanced incentives for new investment in fast-start generation.

Other issues

The AEMC notes in the draft determination that the outlook for generation capacity in the NEM is for an increasing volume of small, 5-30MW generating units, i.e. those that are or could be non-scheduled generators. We agree with the AEMC's outlook and add that in the absence of reform of the thresholds for non-scheduled generation, this is only likely to increase further. This is because there are advantages to remaining a non-scheduled generator such as not being constrained off, not being liable

³ Ibid.

⁴ AEMC, op. cit. p 64.

for FCAS costs⁵ and choosing whether to generate depending on the wholesale price at the time. These outcomes introduce inefficient outcomes into the dispatch, pricing and settlement processes.

Should the AEMC decide to implement the Five Minute Settlement rule change, we would expect that the incentives to remain non-scheduled will only be increased leading to further increases in the already growing capacity of non-scheduled generation.

The Commission also argues that the decision not to make the rule change at this time, does not preclude the thresholds for scheduled generation needing to be examined at some point in the future. It is encouraging that the AEMC appears to acknowledge that at some point the threshold will need to be changed. However, ERM Power considers that this may come too late. It is entirely possible that the AEMC will only act when it is too late, when an increase in market distortion is observed and secure operation of the power system is impacted by larger volumes of non-scheduled generation and price responsive load. Furthermore, this increased level of non-scheduled generation installed in the intervening period would be likely to remain non-scheduled, as retrospectivity in rule changes should be discouraged.

Conclusion

ERM Power disagrees with the AEMC's draft determination not to make a rule change reducing the threshold for scheduled generation from 30 MW to 5 MW. We contend that the most appropriate approach for the AEMC to have taken would be to make the rule change on non-scheduled generation and apply this to new generation with a nameplate capacity greater than 5 MW. This would avoid exacerbating the potential problems with greater volumes of non-scheduled generation.

We also firmly believe that the arguments put forward by the Commission in the draft determination set a precedent that should also apply to the Five Minute Settlement rule change. It would be inconsistent for the AEMC to decide to introduce Five Minute Settlement based on the arguments put forward in this draft determination.

Please contact me if you would like to discuss this submission further.

Yours sincerely,

[signed]

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⁵ The causer pays factors resulting from demand contributions (including non-metered generation) are combined and allocated to a quantity known as the 'residual'. However, NER clause 3.15.6A(i)(2) requires that this residual component be recovered only from Market Customers. This means that non-scheduled generation may not be allocated costs under the current methodology. Under NER clause 2.2.2, only scheduled generating units are required to have adequate telemetry to participate in central dispatch, and as a result, many non-scheduled generating units under 30 MW fall into the category of non-metered generation.