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Transmission Frameworks Review – Second Interim Report

The Energy Supply Association of Australia (esaa) welcomes the opportunity to make a submission to the Australian Energy Markets Commission (AEMC) on its Second Interim Report for the Transmission Frameworks Review.

The esaa is the peak industry body for the stationary energy sector in Australia and represents the policy positions of the Chief Executives of 36 electricity and downstream natural gas businesses. These businesses own and operate some $120 billion in assets, employ more than 51,000 people and contribute $16.5 billion directly to the nation's Gross Domestic Product.

The Second Interim Report sets out the AEMC's refined positions on the three key elements of the Transmission Frameworks Review: generator access; planning and connections. The Commission has proposed some significant changes, in particular the arrangements for generators to access the transmission network. The proposals seek to address a number of ongoing issues with the existing framework, such as the lack of appropriate pricing signals for congestion and the arrangements governing connections.

While the esaa sees merit in the AEMC's proposals there are some concerns in relation to the practical implementation of some aspects of the optional firm access (OFA) model. The esaa believes these issues need to be addressed prior to the AEMC putting forward recommendations to the Standing Council on Energy and Resources.

Generator access

For some generators congestion is adversely impacting their business. Over the next decade the impact of congestion is likely to increase due to the roll-out of significant new renewable plant to meet the Renewable Energy Target.

The AEMC's proposal to introduce access pricing would be one of the most significant changes to the electricity market since the introduction of the National Energy Market (NEM). The proposed model is an elegant solution to the incentives in the market that drive disorderly bidding and would provide a price signal for the location of new generation capacity. The model would remove the incentive to disorderly bid by decoupling access from dispatch. Further, by providing an

opportunity to guarantee access it should improve the liquidity of the contract market and lower the risk and cost of new generation investment.

Given the scale of the change there is unsurprisingly a degree of caution from some members of the industry. There are a number of concerns with the current design of the OFA model that need to be addressed for generators to be able to assess the overall impact of the proposed model, including the pricing methodology, access standards, the transitional arrangements and most importantly whether the benefits of the model outweigh the costs.

The proposed access pricing arrangements are unnecessarily complex. It would be preferable if an alternative simplified model was developed that still retains the aims of the AEMC proposal. Similarly the access standard arrangements would benefit from being simplified.

The AEMC has outlined their position that generators will receive some level of grandfathered access, which will be reduced over time to a certain level until the plant ceases operation. One issue with the current design is the reduction of access after the initial allocation. Based on the available information, it is not clear why a generator's access should taper down after the initial allocation. Given generators have an incentive to use their access rights or to sell them where they are no longer needed, the reallocation of access rights after the initial allocation should be managed through trade.

There is concern among some generators that it will be difficult for them to assess their appropriate level of access. The introduction of access pricing will reduce a risk (congestion) that is currently difficult to manage. The AEMC believes generators already have to manage the risk of congestion, but if they are uncomfortable acquiring access rights they are free to remain on non-firm access (which is equated to the current situation).

The AEMC position is not entirely accurate. It is true generators currently have to manage the risk of being constrained off. However, generators manage this simply by reducing their contract position to allow for some head room (a more passive approach than acquiring additional rights). While there is currently no way to manage the future risk of another generator being built that affects transmission capacity, generators have time to adjust their contract position before a new plant commences operation.

esaa does not agree that non-firm generation can be equated to the current arrangements. Once parties can have firm access, being non-firm could produce quite different outcomes (access would vary by the level of firm access purchased by other generators, rather than the capacity of the network).

At this stage, the AEMC has justified implementation of the OFA model based on how it will work in theory. It will be important to test/simulate how the model will work under real world conditions to make sure it is compatible with the various complexities of the NEM. It will be particularly important to assess the implications for semi-scheduled generators and the impact of other constraints, such as stability constraints and frequency control and ancillary services (FCAS) constraints.

As acknowledged by the AEMC, introducing OFA is likely to be time consuming and potentially costly. This raises the legitimate question whether the cost of congestion and the potential benefits of improved contracting are of the magnitude to justify the changes. The AEMC has committed to undertake some modelling to assess the costs and benefits, but has also warned of the limitations of the exercise given the nature of the change, suggesting that first principles will provide a better guide. While esaa accepts that modelling OFA is difficult due to the uncertainty of forecasting future congestion created by new generation investment, it is important to amass as much evidence as possible on the impact of the OFA model.

Planning

esaa supports the AEMC proposals to improve transmission planning. Enhancing the role of the Australian Energy Market Operator (AEMO) as the National Transmission Planner is a positive step, as long as transmission network service providers (TNSP) retain responsibility for the work that needs to be carried out at the local level to deliver transmission services. Having AEMO provide advice on TNSP planning and investment tests reports should improve consistency and facilitate consideration of cross regional opportunities. However, care will need to be taken to ensure this process does not become unnecessarily onerous and time consuming. This also applies to the proposed approach to demand forecasts.

Cost reflective pricing will be an important element in providing incentives for TNSPs to examine options in other regions to meet reliability requirements. As a general principle, cost reflective pricing should drive more efficient outcomes. Ensuring that the cost of transmission investment is borne by the geographic areas that benefit, regardless of their location, should lead to better outcomes.

If the AEMC's planning changes are adopted it will have implications for AEMO's role in Victoria. esaa agrees with the AEMC's view that having a consistent approach across the NEM is desirable (i.e. aligning Victoria with other jurisdictions by assigning planning responsibilities to SP AusNet). Further, esaa agrees that "financial incentives are likely to provide the most robust and transparent driver for efficient decision making" and hence support the owner-operator being responsible for planning and investment decisions.

Connections

As a general rule competitive tensions will drive better outcomes and markets are better served by having well informed participants. As such, esaa supports greater competition and transparency where they provide for a more efficient outcome. However, a balance does need to be struck between competition and the need to maintain the operational integrity of the transmission system. In situations where competition is not a viable option, regulation should be designed to afford as much flexibility as possible to the negotiating parties.

Any questions about our submission should be addressed to Kieran Donoghue, by email to kieran.donoghue@esaa.com.au or by telephone on (03) 9205 3116.

Yours sincerely

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