



21 October 2021

The Commissioners  
Australian Energy Market Commission  
PO Box A2449  
Sydney South NSW 1235

Sent to: AEMC by online lodgement.

Dear Commissioners

**Capacity Commitment and Synchronous Services Markets  
Response to Directions Paper  
ERC 0306**

Major Energy Users Inc (MEU) is pleased to provide its thoughts on the directions paper relating to the proposed rule changes for capacity commitment (for access to operational reserves and security and reliability services) and synchronous services (including inertia, voltage control and system strength) markets.

The MEU was established by very large energy using firms to represent their interests in the energy markets. With regard to all of the energy supplies they need to continue their operations and so supply to their customers, MEU members are vitally interested in four key aspects – the cost of the energy supplies, the reliability of delivery for those supplies, the quality of the delivered supplies and the long-term security for the continuation of those supplies.

Many of the MEU members, being regionally based, are heavily dependent on local staff, suppliers of hardware and services, and have an obligation to represent the views of these local suppliers. With this in mind, the members of the MEU require their views to not only represent the views of large energy users, but also those interests of smaller power and gas users, and even at the residences used by their workforces that live in the regions where the members operate.

It is on this basis the MEU and its regional affiliates have been advocating in the interests of energy consumers for over 20 years and it has a high recognition as providing informed comment on energy issues from a consumer viewpoint with various regulators (ACCC, AEMO, AEMC, AER and regional regulators) and with governments.

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The MEU recognises that the change in generation mix (especially the increased share of asynchronously connected variable renewable energy (VRE) generators) in the NEM is resulting in some negative impacts on the electricity supply system and that some actions are needed to ensure that the supply system is maintained in a secure and reliable state. Because of the transition, there are some essential services that are currently provided “free” by synchronous generation which are not so provided by asynchronous VRE generation, (which are also consumers these essential system services) and so there is an increasing need for these to be provided separately, whether by direction from AEMO (as occurs now) or as a separate service.

The purpose of the Directions Paper is to assess to what extent these system services are required and the best mechanism to deliver them in the most efficient manner, whether by a market-based approach (as market ancillary services – MAS) or on a non-market-based approach as non-market ancillary services – NMAS. However, in the directions paper, there is an assumption that implementing a mechanism to provide these system services (instead of the current process where AEMO issues directions to synchronous generators to ensure the services are provided) is the preferred option. There needs to be an assessment as to whether implementing a new mechanism for the provision of these system services actually provides a net benefit to consumers compared to continuing with the current approach, and such an assessment needs to exclude notional benefits that might be delivered in the energy spot market as there is no certainty that there will be lower spot or retail prices as a result of implementing a process for providing these new services.

An alternative approach to ensuring the provision of these essential services that has not been considered, is to amend the Rules to implement a beneficiary pays approach for cost recovery of directions for providing power system services. As asynchronous VRE generators are the beneficiary from the provision of these services, allocation of the costs to them might provide an interim least cost framework for the provision of the services and provide time and the economic incentives for the implementation of self-supply of system services by VRE, the same as that currently provided “free” by synchronous generators – such an approach would effectively impose technology neutrality between different generator types, a goal that underpins the NEM rules.

The MEU recognises that these issues (delivery of essential services) were discussed at length during the development of the ESB post 2025 electricity market report to governments, and the ESB’s Final Report indicates a preference for such essential services to be provided on a non-market-based approach. The MEU considers that, if an alternative to the current arrangements can be demonstrated to be a lower cost solution, along with the AEMC, this ESB approach is preferable, although the MEU considers that there must be some controls to ensure there is some competition in their provision. So far, there has been little examination of the most effective manner of their provision, who should pay and how they interact with the provision of other essential services, such as system strength and fast frequency response, which are already subject to separate rule change processes.

The MEU also notes that a market-based approach to providing these services might provide more efficient outcomes, but would probably require considerable change to the market dispatch engine (NEMDE) to ensure that the dispatch of both the energy

supply and the essential services were optimised to deliver the most efficient outcome for consumers. Additionally, the MEU recognises that:

- Continuation of the current AEMO practice of issuing market directions to maintain system security of the market is both increasing in frequency and at considerable additional direct cost to consumers, so establishing a formal approach to the delivery of the essential services could result in lower costs for consumers on the basis that separate acquisition of these services should cost less than continuing with ad hoc directions, although as noted above, although this assumption is still yet been proven.
- The electricity supply market is still concentrated (ie has limited competition – possibly workable competition) and it is imperative that provision of system services via a new mechanism does not reduce competition in the delivery of energy, FCAS or the essential system services themselves.

These three observations support the MEU view that, absent a change to the cost recovery for the current directions framework, a non-market-based approach for the delivery of the essential services is preferable to a market-based approach, at least in the short to medium term, while the development of the NEM processes to best manage the transition to asynchronous VRE generation continues. Ultimately, it is possible that when the NEM reaches a level of maturity where the bulk of the energy supply is provided from asynchronously connected VRE, an overall market ancillary services-based solution for the supply of all essential services, including the self-supply of these system services by asynchronous generators, might well deliver the best outcome for consumers. Until that time, the MEU considers that a non-market-based approach is more likely to achieve the National Electricity Objective (NEO) than a market-based option.

As with the need for provision of system strength in the networks, the need for these rule changes was caused by increasing asynchronous VRE in the market and the MEU sees that the need to provide these additional essential services is driven by the methods used by the VRE generation in their processes used to supply energy. While the costs implicit with the draft rule for the provision of the system strength initially lies with consumers (a position that the MEU did and still does not support), it does provide a mechanism for the recovery of at least some of the costs from those that caused the need. Further, the MEU considers that not only has asynchronous VRE caused the need for increasing levels of system services, but the provision of these additional essential services will allow the VRE generators to be more productive and profitable, highlighting that VRE are the primary beneficiaries of the provision of these system services. The MEU therefore considers there needs to be an approach of cost recovery applied to the costs incurred for providing these additional essential services from the causer and beneficiary of the need (ie asynchronous VRE generation).

The MEU is concerned that there is consideration in the Directions Paper of a mechanism that incorporates both unit commitment security (UCS) and a system security mechanism (SSM) as a solution for the provision of these essential services. The need for these essential services occurs in near to real time whereas the UCS approach forecasts needs years in advance,(ie in the “planning” domain) and therefore contracting for UCS would impose long term commitments and potentially

unnecessary costs. In this regard, there is no clarity on when (or even if) UCS might be triggered and so it is possible that a UCS provider might be unnecessarily removed from providing into the energy market if their participation is dependent on activation of a UCS contract. We also note that contracting for system strength services by network service providers would also occur in the “planning” timeframe, and this may result in competition between AEMO and network service providers for procurement of system services. With this thought in mind, there needs to be greater clarity on the timing needed for provision of these services as part of the assessment as to whether UCS or SSM or both, are needed to ensure the ongoing provision of the services.

The MEU sees that the Short-Notice RERT Panel process provides a guide for a potential model in the provision of these essential services, as it has a panel of providers established with pre-agreed contract conditions and prices, and which can be dispatched at short notice, but unless they are actually dispatched, they remain free to provide other services including energy and FCAS. The approach for provision of these services should, as with RERT, limit the level of discretion available to AEMO in its processes.

While it is accepted that there is an increasing need for the provision of these essential system services, there is no clarity as to the services required and the level or quantum for these services at any particular time. The MEU understands that AEMO currently provides these services in a “bundled” format under its directions program. The MEU understands that the AEMC technical working group has sought improved transparency in this area via requests for additional information from AEMO regarding the components of the services required to facilitate unbundling of the services (and their costs), but this request has not been addressed by AEMO. In order to develop a tool for assessing the need, timing, and quantum for each of the additional system services, it is imperative that there be greater transparency about what is needed, when it is needed and in what amount. Without this greater transparency, it is impossible to assess what the demonstrable net benefits will be from the separate provision of the services and whether the approach finally determined is indeed the most efficient method, or even if the change from the current AEMO directions process results in a lower cost solution.

The MEU is also concerned that with TNSPs being responsible for the procurement of system strength contracts which could involve generators providing the service, there needs to be close coordination between TNSPs and AEMO so that there is no overlap or the ability for “double dipping” in the provision of the services. This means that the TNSP contracts for providing system strength (and other system services) must have a high degree of transparency both of the system strength contracts but also those for the provision of the required services by AEMO. Included in this transparency must be the times and the durations the contracts require the services to be available, when they are activated and deactivated, in which regions and the volumes involved.

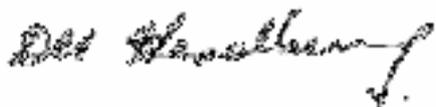
Overall, the MEU considers that:

- Consideration should be given to implementing a simple rule change in the area of cost recovery for system services directions. This may be a relatively low cost and efficient change and may provide the least cost option

- There needs to be an assessment as to whether the costs for NMAS or MAS provide a net benefit for consumers compared to the current “directions” approach other than a view that lower spot prices might eventuate
- If proven to be needed, based on the current information provided in the Directions Paper, NMAS is preferred to MAS for at least the short to medium term
- Cost recovery for provision of these system services needs to reflect the reality that it is asynchronously connected VRE generation that has caused the problem (and therefore should pay to fix it) and that asynchronous VRE is a beneficiary as the provision of the services will result in improvements in their dispatch and profitability
- Care must be taken to ensure that the new services do not lead to any reduction of competition in the energy or FCAS markets and that there is adequate competition for the provision of the new services
- The MEU does not see a need for both UCS and SSM, and considers that SSM alone should be adequate without locking in the long-term contracts implicit in UCS
- There needs to be “unbundling” of the different services to identify the actual need for the services, including the quantum of each service needed, and its timing in terms of time of year, time of day, etc. This information is needed to assess the benefits and the costs involved so that the most efficient approach can be identified
- The MEU considers that the NMAS should be provided similarly to the Short-Notice RERT Panel framework as this is a process that is well known and operates reasonably well
- Where system services are dispatched to achieve a notional market benefit, special reporting obligations should apply where AEMO provides information about which additional system services were being dispatched and what market benefit/disbenefit was actually achieved.
- Care needs to be taken to ensure there is no overlap, conflict, or double dipping when the AEMO process operates alongside the TNSP processes for system strength

The MEU is happy to discuss the issues further with you if needed or if you feel that any expansion on the above comments is necessary. If so, please contact the undersigned at [davidheadberry@bigpond.com](mailto:davidheadberry@bigpond.com) or 0417 397 056.

Yours faithfully



David Headberry  
Public Officer