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Ben Hiron

Australian Energy Market Commission

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28 October 2021

Dear Ben,

Primary frequency response incentive arrangements draft rule

AGL Energy (AGL) welcomes the opportunity to comment on the Australian Energy Market Commission (AEMC) Primary frequency response incentive arrangements draft rule determination.

AGL is a leading integrated essential service provider, with a proud 184-year history of innovation and a passionate belief in progress – human and technological. We deliver 4.2 million gas, electricity, and telecommunications services to our residential, small, and large business, and wholesale customers across Australia. We operate Australia's largest electricity generation portfolio, with an operated generation capacity of 11,208 MW, which accounts for approximately 20% of the total generation capacity within Australia's National Electricity Market.

AGL does not support the AEMC's draft decision to make mandatory primary frequency response (PFR) permanent. We suggest the AEMC instead implement an effective PFR incentive mechanism which drives PFR provision by market forces and has the capability to specify minimum regional quantities to ensure the Australian Energy Market Operator (AEMO) has confidence that adequate PFR is being provided. We suggest that further consultation will be necessary to complete the design of an effective mechanism. If these suggestions are not possible, we suggest the AEMC make a final determination to extend the mandatory PFR sunset date to June 2025. This would ensure AEMO has certainty that adequate PFR is being provided in the short term but also allow the AEMC adequate time to review the need for a PFR mechanism as the energy mix changes.

Mandatory PFR

AGL does not dispute the benefits of widespread narrow band PFR, especially as the supply mix becomes increasingly decentralised, inverter-based, and variable. However, we suggest that this can be achieved without mandatory PFR. Widespread, geographically dispersed PFR, does not require mandatory provision of PFR as evidenced by the fact that the system frequency stabilisation benefits since the introduction of mandatory PFR did not increase significantly after around 30% of scheduled and semi-scheduled generators in the NEM had implemented PFR. In addition, PFR sourced from mandatory provision means that PFR will be provided by whatever units are dispatched to provide energy in a given interval no matter their location. As a result, mandatory PFR may at times provide less geographic dispersion than an alternate mechanism which could overcome any system operator concerns regarding the amount or location of PFR provision by specifying minimum regional quantities.

Under mandatory PFR, instead of sourcing PFR from the units that can most efficiently provide it, those that cannot provide it efficiently will be forced to provide some, which will displace the provision by the efficient providers. This will mean that the cost of providing PFR will be greater than it should be and also that plants which have a high capability to provide PFR may not receive sufficient incentives to ensure adequate PFR capacity in the market. We note that the AEMC and Greenview Strategic Consulting have indicated that they are concerned by potential future low PFR capacity in the future and have therefore suggested new frequency responsiveness reporting obligations for AEMO. While we support these reporting obligations, we suggest that ensuring future frequency responsiveness would be better managed by ensuring that an effective enduring PFR mechanism is implemented.

AGL suggests that rather than cancelling the proposed June 2023 mandatory PFR sunset date, the AEMC move the sunset date to June 2025. We are concerned that the current PFR mechanism is being assessed in the context of the current state of the NEM without adequate regard to the expected exit of large synchronous generators, including the 2023 exit of AGL's Liddell Power Station. Due to these exits, and the energy transition generally, we expect that NEM PFR requirements will become more reliant on provision from wind, solar, and batteries. By setting a new sunset date the AEMC would have an obligation to reassess PFR requirements as the new post-exits context emerges, which will ensure that the assessment occurs in a timely fashion, rather than the potential situation where problems begin to emerge and then a new solution must be implemented quickly without the opportunity to fully consider all options.

Reforms to the causer pays process

AGL supports payments for PFR to ensure the existence of an investment and provision incentive for this essential system service, and also to provide compensation for forgone generation and FCAS revenues.

We consider that the proposed causer pays reforms require further development. We note that there seemed to be significant confusion amongst stakeholders how the performance payments will operate, and it is not clear that the performance payments will provide adequate compensation to drive investment. AGL is particularly concerned that the proposed process may require companies with generation portfolios with very low or zero regulation FCAS recovery costs to have a significant increase in costs even though are not contributing to the regulation FCAS requirement. It is also not clear that the proposed mechanism will ensure adequate provision of PFR after large synchronous generators exit the NEM. We note that an incentive payment for something for which provision is mandatory is unlikely to adequately drive investment behaviour. We suggest that the AEMC give further consideration to alternate PFR incentive options including the AEC/ARENA funded Double-sided causer pays project completed by Intelligent Energy Systems and also a pure PFR market design where PFR is procured in a similar manner to regulation FCAS.

AGL considers that more time is required to fully develop an appropriate causer pays mechanism. The proposed mechanism did not benefit from adequate consideration by the AEMC Frequency Technical Working Group (TWG) or multiple rounds of industry consultation. We suggest that achieving broad support from the TWG for the mechanism should be an objective for further consultation. The current proposal leaves significant high-level design for the mechanism in the hands of AEMO, we consider that this design should more appropriately be completed by the AEMC in consultation with stakeholders.

New reporting arrangements

The draft rule requires AEMO to report on its assessment of quarterly aggregate frequency responsiveness, and AER to report on the total costs of frequency performance payments for each region. AGL supports the new reporting arrangements as we expect the need for, and cost of, primary frequency response to grow in the NEM as the system transitions and more thermal exits take place.

Timing and implementation

Due to the concerns expressed above, AGL suggests that further consultation is necessary before the AEMC makes a final determination. While this will delay the implementation of incentives for PFR we accept this delay as it is important that the best incentive mechanism is implemented. We do not otherwise support a delay in appropriately compensating PFR given the need for clear investment signals, and therefore suggest the proposed implementation timing should be truncated. We suggest that a total of 18 months, rather than the suggested 27 months, should be adequate since PFR is already being provided without compensation and because the implementation of PFR incentive payments should not take longer than the 18 months required to implement Fast Frequency Response.

If you have any queries about this submission, please contact Anton King on (03) 8633 6102 or aking6@agl.com.au.

Yours sincerely,

Chris Streets

Senior Manager Wholesale Markets Regulation