24/600 Bourke St
Melbourne VIC
3000

23 February 2023

Ms Anna Collyer
Chair, Australian Energy Market Commission
GPO Box 2603
Sydney, NSW, 2001

Via electronic lodgement: https://www.aemc.gov.au/contact-us/propose-rule-change

Re: Rule Change Request – Recovery of Funds for Capacity Directions

Dear Ms Collyer:

Tilt Renewables submits the attached rule change proposal under section 91 of the National Electricity Law.

The attached rule change request proposes to:

- Change the recovery of capacity directions from both generators and customers to solely customers so that the benefeciary of the capacity direction is financially responsible for the liability it creates.

Thank you for taking the time to consider this fast-tracked rule change request, and we look forward to continuing discussions with the Commission on these issues. Please feel free to contact rhys.albanese@tiltrenewables.com should you have any questions or wish to discuss any aspect of this submission.

Yours Sincerely,

Rhys Albanese

Market Operations Manager

Tilt Renewables

24/600 Bourke St
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Rule Change Proposal: Recovery of Funds for Capacity Directions

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1. Request to make a rule change

1.1 Name and address of person making the request

Tilt Renewables
Bourke Place
24/600 Bourke Street
Melbourne VIC 3000

2. Background

2.1 Tilt Renewables

Tilt Renewables is committed to continue playing a lead role in accelerating Australia's transition to clean energy. Tilt Renewables is one of the largest owners and operators of wind and solar generation in Australia with 1.7 GW of renewable generation capacity across 12 operating (or under construction) wind and solar farms. In addition, Tilt Renewables has a development pipeline of over 5.0 GW of wind, solar and storage projects.

2.2 Background to the Rule Change Request

Over the course of the last several years the generation mix in the NEM has evolved with significant new entry from VRE (Variable Renewable Energy) at both a grid-scale and distribution level. Market dynamics that were closely linked to temperature as a result of heating and cooling load have now come more complex, with wind and solar irradiance becoming increasingly influential in determining price and demand outcomes. The volatility that has since ensued in market prices and fuel prices, along with the higher cost of building dispatchable generators compared to VRE has stifled investment in new dispatchable capacity coming online.

The recent market volatility which occurred over the winter of 2022 saw the market price cap set in every NEM region along with a suspended market with administered pricing[1], largely driven by extremely high fuel prices and generators withdrawing supply due to the administered price cap. AEMO also directed pumped hydro load online in order to clear Lack of Reserve conditions and provide further reliability to the system[2]. Whilst the previous winter is not the first time AEMO has directed for capacity, it is the first time it has done so with a material cost, in this case totalling $9.64 million for pumped hydro directions alone.

Given the pumped hydro load directions were not interpreted by AEMO to be an energy or an ancillary service direction, the recovery of such amounts align with the recovery of other compensable amounts under clause 3.15.8(g) of the NER (National Electricity Rules). Such

[1] Refer to: Market Suspension FAQs – June 2022 (aemo.com.au)
[2] Refer to: 1 (aemo.com.au)

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amounts are recovered from both market generators and market customers. This is different to the recovery of energy and ancillary service directions, which are recovered from customers under clause 3.15.8(b) of the NER.

3. Statement of Issue

The events of winter 2022 under which AEMO issued directions to pumped hydro loads for the purposes of securing spare capacity was funded by both generators and loads, however the sole beneficiary of the capacity directions were customers which were afforded greater reliability. There is an inefficient allocation of risk at play here whereby generators who made themselves available during low reserve have ended up with part of the cost recovery bill for capacity directions.

The NEM has traditionally used a cost allocation structure whereby the causer of the cost is financially responsible, for example we see this in cost allocation for FCAS recovery and more recently with the System Strength Impact Assessment Guidelines. This scenario whereby generators are contributing for capacity directions which solely benefit customers seems to be an exception and inconsistent with cost allocation principles that have underpinned the NER. A further example of this which is also used to improve reliability for consumers is RERT, which is also recovered from customers.

4. Proposed Rule Change

4.1 Description of Proposed Rule Change

Tilt Renewables is proposing a rule change such that customers are solely responsible for the recovery of capacity directions payments in the NEM, similar to energy and ancillary service directions, which are recovered from customers under clause 3.15.8(b) of the NER. This can be done by either changing clause 3.15.8 of the NER or explicitly defining capacity directions as a form of energy direction, such that these directions are recovered under clause 3.15.8(b) rather than clause 3.15.8(g).

As customers are the beneficiaries of increased reliability of supply, it is appropriate that they cover the compensation amount, similar to energy directions, ancillary services directions and RERT (Reliability and Emergency Reserve Trader) directions.

While some may argue that generators benefit from increased demand through increased wholesale prices, directed capacity providers can then provide zero cost generation at a later point in time to the opposite effect as a result of the compensation. Furthermore, given capacity providers can also claim startup costs and opportunity costs that would otherwise be recovered through normal business operations, there is no benefit to generators with respect to these startup costs. Tilt Renewables therefore considers this argument moot.

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4.2 How the Proposed Rule Change Will Address the issue

This proposed rule change request seeks to correct an inefficient cost allocation that exists within the NER whereby cost recovery for capacity directions is partially covered by generators. As mentioned previously in the paper, customers are the beneficiaries of capacity directions due to enhanced reliability and should therefore be financially responsible for this outcome.

Charging generators for these directions doesn't create the right incentives to alter generator or consumer behaviour. Generators are naturally incentivised to make themselves available during low reserve conditions through expected higher wholesale prices. The correct cost allocation of capacity directions would incentivise customers and retailers to be more responsive through mechanisms such as demand response.

Lastly, many generators are also developers who invest in new generation and thereby increase reliability. The amount that generators are charged for capacity directions is capital that isn't invested in new generation and energy storage facilities.

4.3 How the Proposed Rule Change contributes to the National Electricity Objective

This proposed rule change seeks to address inefficient risk allocation relating to the costs associated with capacity directions for enhanced reliability in the NEM. Aligning payment with benefit is the most efficient outcome with respect to capacity directions. Not only does this philosophy underpin many of the other cost allocations of the NER, it also works to incentivises efficient behaviours, the demand response argument mentioned previously is an example of this.

Ensuring that efficient cost allocations in place will also promote investor confidence and ensure that more funds are available for developers to invest in new supply and storage infrastructure, increasing reliability within the NEM and reducing the likelihood of further directions from AEMO for capacity.

5. Expected Costs

Compensation calculations are completed on an ad-hoc basis by AEMO. Given that AEMO is already able to charge customers for directions under clause 3.15.8(b) of the NER, Tilt Renewables expects system change costs to be immaterial, particularly in comparison to recent and any ongoing capacity direction payment amounts.

Consumer costs relating to payments for capacity directions would increase under this proposed rule change, however the main argument of this rule change request is that this cost is most efficiently allocated to consumers, as they are the sole beneficiary of these directions and can influence demand outcomes from demand response.

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