



17 January 2014

Mr Neville Henderson
Chairman
Australian Energy Market Commission Reliability Panel
PO Box A2449
Sydney South NSW 1235

Submitted online: www.aemc.gov.au

Dear Mr Henderson

RELO051: RELIABILITY STANDARD AND SETTINGS REVIEW 2014

Origin Energy (Origin) appreciates the opportunity to comment on the Draft Report that has been prepared by ROAM Consulting (ROAM) for the Australian Energy Market Commission's (AEMC's) Reliability Panel (Panel), the substance of which was discussed at the public forum on 4 December 2013.

At a high level, ROAM has applied a 'cap defender' modelling approach, in addition to its previous 'extreme peaker' approach, and has stated that the former is the preferred approach for the review. While we consider ROAM's preferred methodology to be a more reasonable starting point, we emphasise that the cap defender approach, like the extreme peaker approach, yields a highly artificial representation of the market, as has been acknowledged by ROAM in its Draft Report:

- Modelling is performed on a trading interval basis¹
- Fair value cap contracts are assumed²
- Pool price outcomes are post-processed to apply a different MPC and CPT to all regions simultaneously³
- Pumped hydro schemes with relatively short-term storage are particularly influential⁴
- Generation is retired to the point that unserved energy conditions are achieved across all regions, and ROAM acknowledges that a number of market participants have expressed concern with this approach as it is not reflective of what would occur in reality⁵

More broadly, the significant discrepancy between the outcomes of the two modelling approaches, in terms of the settings required to deliver the standard, suggests that consideration of specific modelling outcomes ought to be tempered by empirical evidence of market operation. For example, if the current settings are observably

¹ ROAM acknowledges that under this methodology it is not capturing the volatility which results from dispatch interval effects such as ramp rates and fast start inflexibility profiles and that it assumes that the OCGI is always able to fully capture price volatility that does occur, excluding periods when the unit is on random or planned outages; Draft Report p 27

² ROAM has not accounted for cap contracts trading at any premium above their fair value; Draft Report p 27

³ As a consequence, the impact of a lower MPC in one region, and its associated impact on investment incentives, was not taken into account when determining the revenue of the cap defender in another region; Draft Report p 33

⁴ A conservative modelling approach means that the presence of substantial hydro generation in New South Wales, Victoria and Queensland contribute to the reduced MPC required to achieve the reliability standard, as compared to South Australia; Draft Report p 38

⁵ In particular, a number of market participants have argued that the assessment of a new entrant is inappropriate in a market that has sufficient capacity installed to just meet the reliability standard; Draft Report p 5

delivering the standard to date, then it would be prudent to question modelling outcomes that suggest that they will not do so in the future.⁶

We therefore consider that the outcomes of ROAM's modelling ought to be viewed in light of the abstract assumptions such modelling requires. In particular, any modelling outcomes that suggest that a significant departure from the current settings is warranted ought to be considered in the context of the finding implicit in ROAM's Draft Report that the current settings have been effective in delivering the standard.

We provide further comments in relation to several specific modelling assumptions below.

Reliability Standard

ROAM has noted that the cap defender approach creates a significant disparity between regions in relation to the MPC required to achieve the reliability standard, but that there would be very significant challenges in the application of different reliability settings in each region. Given the impacts this approach would have on the market are potentially significant and largely unknown, ROAM proposes that these difficulties outweigh the possible economic benefit that may result from a regional application of reliability settings. This is consistent with the view of the Panel during the 2007 review,⁷ and we agree that a consistent reliability standard across the regions is preferable.

Demand side response

ROAM will apply peak demand and energy forecasts published by the Australian Energy Market Operator (AEMO) in the 2013 National Electricity Forecasting Report (NEFR), which assumes that a demand response mechanism (DRM) is implemented. While the volume of demand response assumed by ROAM does not have a significant impact on the results, in our view the design of the DRM that is currently proposed is highly problematic and therefore we consider that any assumptions flowing from implementation of the DRM should be treated with caution. In this regard, we note the recent decision by the Standing Council on Energy and Resources to request that AEMO defer lodgement of a rule change request to implement the DRM to allow for further work, including a cost benefit study.

Carbon and LRET policy

ROAM proposes to model the current LRET in the central scenario, which represents approximately 41TWh of renewable generation by 2020 Australia-wide, and to use the carbon repeal trajectory as the central trajectory when analysing sensitivity to demand, renewable energy target, gas price and demand side participation. We consider that carbon pricing and renewable energy scheme assumptions ought to be treated with caution in the current policy environment.

⁶ This is consistent with ROAM's proposal that 'it is not the intention of these reviews that the MPC (and potentially the CPT) fluctuate wildly based on the surplus or shortage of supply at the time of each review'; Draft Report p 5

⁷ The Panel noted that a hybrid standard had been rejected in 1998 and that it was 'still of the view that, on balance, introducing multiple forms of the reliability standard would be detrimental because it removes the simplicity offered by a single form, would be difficult to justify on economic grounds, and has the potential to distort or dilute investment signals'; AEMC Reliability Panel, Comprehensive Reliability Review, Final Report, December 2007, p 24

Should you have any questions or wish to discuss this information further, please contact Sarah Paparo on (02) 9503 5300 or sarah.paparo@originenergy.com.au.

Yours sincerely,

A handwritten signature in blue ink that reads "K. Robertson". The signature is written in a cursive style with a horizontal line at the end.

Keith Robertson
Manager - Regulatory Policy