2 September 2014

Mr John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Dear Mr Pierce

Alinta Energy welcomes the opportunity to make a submission in response to the *Optional Firm Access, Design and Testing*: *First Interim Report* (the Report) and appreciates the detailed work undertaken by the Australian Energy Market Commission (AEMC) to date.

Alinta Energy is an active investor in the energy retail, wholesale and generation markets across Australia. Alinta Energy has around 2500 megawatts of generation capacity in Australia (and New Zealand) and a growing retail customer base of over 750,000.

Alinta Energy is a member of the industry working group hosted by the AEMC.

Discussion

Alinta Energy has long held concerns regarding generator access to transmission and has reiterated that the risk of asset stranding, and significant and unmanageable congestion pose a threat to existing and new investors alike.

Further, that while these risks are less concerning for larger entities with significant and geographically dispersed portfolios, second tier and new entrant competitors are likely to benefit from being able to better manage secure access to transmission for the life of their investments (or an agreeable and known timeframe) across all technology types.

Alinta Energy supports the work of the AEMC in addressing the issues raised by various companies in the years prior, over the course of the *Transmission Frameworks Review*, and currently as part of *Optional Firm Access, Design and Testing* review.

Overall, Alinta Energy contends that the case for change has been made but that it is unclear if all aspects of the Optional Firm Access model (OFA) can be justifiably implemented at this point in time. As such, Alinta Energy supports an abridged approach that would facilitate possible staging over the longer term and ensures that the no regrets elements of the OFA model can be implemented regardless.

<u>AEMC preference for OFA</u>

A number of options for addressing generator access to transmission were considered during the *Transmission Frameworks Review*; however, the AEMC's preferred approach was and remains the OFA. The AEMC notes that:

> *The optional firm access model would introduce more commercial drivers on transmission businesses, and more commercial financing of transmission infrastructure. This approach should minimise the total system cost of building and operating both generation and transmission over time, and so potentially minimise prices for electricity consumers in the longer term.*
>
> (AEMC, *Optional Firm Access, Design and Testing, First Interim Report*, pg. 1)

Alinta Energy agrees with these claims; at a conceptual level OFA is an appealing model which provides a range of potential benefits as documented in the Report. Whether all these benefits can be achieved in practice is more uncertain.

Unfortunately, the AEMC has long held the view that OFA core features cannot be deviated from and that the industry faced a binary choice: implementation of OFA in its entirety or no change from the status quo. The fact OFA core features have since been amended by the AEMC and that alternatives to the OFA model exist in numerous other jurisdictions, domestically and internationally, suggests the AEMC's position is unhelpful.

The AEMC's all or nothing approach is concerning, as it strongly suggests that if one component of the OFA is unsatisfactory or difficult to justify, all possible reforms to generator access to transmission will be abandoned.

Alinta Energy has consistently argued that while the AEMC is encouraged to progress analysis of the entire OFA, it should not be the case that aspects of the proposals that will deliver benefits of themselves should not, or cannot, be advanced in isolation.

Notably, in response to Australian Energy Market Operator's assessment of dispatch outcomes under OFA, Alinta Energy now sees fewer benefits in amending access settlement at any time in the near future. Alinta Energy appreciates that this may be a result of the inherent difficulties in modelling market outcomes, as opposed to a reflection on the incremental benefits of access settlement, but notes that without a clear understanding of settlement impacts via a more substantial trial, or more certain modelling, the case for changing settlement has been dealt a serious blow.

In addition to AEMO's inconclusive analysis of dispatch outcomes, the experiences of the working group, where complexities have been raised, poses questions about the scale of the changes required to implement OFA. This does not mean Alinta Energy supports abandonment of the reform process. That said, given the AEMC's all or nothing position it is difficult to envisage the AEMC garnering much, if any, industry support for the OFA in the form it has been presented.

This gives rise to the circumstance where OFA has no strong advocates in industry and is seen largely as a creation of the AEMC which is looking less and less likely to be able to deal with the issues raised by industry at the commencement of the *Transmission Frameworks Review.* In this environment Alinta Energy must dispute the position taken by the AEMC that the totality of OFA is the only available alternative to the status quo as it undermines the potential for modest incremental reform.

The AEMC needs to reconsider whether its approach has been or remains appropriate.

Key Consideration: Would a simplified, less ambitious, approach by the AEMC have been more desirable during the *Transmissions Frameworks Review*, and if so, why not adopt a more modest approach now?

Can OFA be scaled back to first principles, even if it is less elegant?

The circumstance in which the AEMC, and industry, currently find themselves, assessing a proposal that represents a very large, very significant, and untested change to the market is less desirable than incremental change and not reflective of the concerns raised and approach outlined by numerous generators over the course of the past decade.

Since prior to the commencement of the *Transmission Frameworks Review*, recognition at the planning level has been the driving concern for Alinta Energy and many other companies. The reasons for this have been previously articulated.

- The absence of obligations on the transmission network service provider (TNSP) to upgrade or maintain the line to remote assets, or generation assets per se, is an oversight in the National Energy Market that Alinta Energy believes require rectification regardless of OFA.
- The current market arrangements for generator access for transmission favour large participants over smaller participants. The size of Alinta Energy's portfolio means unlike large participants it does not gain the advantage of a natural hedge against constraints which provide rents.
- The lingering prospect of increased wind penetration including as a consequence of the committed upgrade of the Heywood interconnector and any potential future policy developments is most significant in South Australia but suggests changes to the way in which the market will evolve more generally.
- Additionally, Alinta Energy's remote position in the South Australian region means the risk of asset stranding is likely to be more significant subject to certain market scenarios.

The OFA is not solely directed at these primary concerns as it deals with a wider range of issues, which while understandable, now threatens the viability of any moderate measured reform that would go a long way to satisfying generators without requiring wholesale market reform.

Alinta Energy suggests that a scaled back OFA which addressed the initial concerns raised by industry participants be considered prior to the Second Interim Report recommending any further course of action on OFA package as it stands.

Key Point: Given the process that has been adopted, the AEMC cannot recommend abandonment of the OFA in its entirety without first considering the scope for more moderate reform based on elements of the OFA model.

A move back to first principles

When Alinta Energy and a number of other companies progressed discussions of generator access to transmission the favoured model was recognition of generator access in the planning domain to manage drivers of congestion in the long-run.

This concern arose out of a view that, primarily, congestion is driven by dynamic decisions that cannot be readily changed in the short run. These concern plant size, locational decisions, and network capability, namely: transmission and generation investment decisions.

In other words, the primary drivers of congestion are determined by business and regulatory decisions which, given the nature of the investment required to develop generation capacity, cannot be easily amended or revised. As such, dynamic efficiency, which concerns the efficiency of long run decision-making and market performance, in timeframes where infrastructure can be changed, is

critical to ensuring inefficient congestion does not unexpectedly arise and is more relevant than managing short-term constraints that arise from time to time.

Revisiting the AEMC's reasons for refuting this model is telling. The AEMC essentially cited the lumpy nature of transmission investment and the potential impost on new entrants as compared with existing generators. However, under the OFA these two issues remain plus there are additional complexities. This is largely a consequence of the OFA ambitiously seeking to provide a holistic solution to a broader set of issues than other approaches.

It is arguable that a move to a simplified version of OFA, at least in the first instance, would ameliorate a number of the industry's concerns and act on the initial issues raised by proponents.

Key Point: Dealing with factors that drive congestion in the long-run is generators main concern and is feasible under a simplified form of OFA.

Retaining the cloak of OFA

Alinta Energy suggests the focus of OFA should be on ensuring recognition of generator access rights in the planning domain and better linking those rights with TNSP incentives (discussed below). This offers a simplified model that does not interfere with access settlement.

The simplified model would also require an appropriate charging methodology for new entrants, noting deep connection costs had previously been proposed. Should deep connection costs not be desirable, alternative charging mechanisms exist; a long-run incremental cost model is one example and Alinta Energy appreciates that the AEMC has invested significant time in investigating this charging approach.

The use of a long-run incremental cost approach to recognition in planning domain, without consequent access settlement, can be calculated based on the AEMC's existing work; however, it is noted that the value of access rights may be less than otherwise would be the case.

The benefits of a simplified model is there would be little need to consider short term access, no changes to access settlement, few concerns with transition and no need to scale grandfathered financial access rights which will only need to be provided in the planning domain. Alinta Energy does not doubt that the AEMC would wish to limit "life of the asset" recognition in the planning domain; this would need to be a matter for discussion

Firm access operating standard

Under an approach that relies on the firm access planning standard in the planning domain and doesn't impact access settlement there is still scope to better incentivise TNSPs. It may be possible to measure TNSP performance against a firm access operating standard to increase incentives and revenue at risk; however, doing so without impacting settlement. This is likely to be supported by industry as a means of improving regulated incentives.

Whether this can occur under the auspices of the service target performance incentive scheme, to simplify implementation for the Australian Energy Regulator, rather than creating a new scheme in its entirety is also worthy of consideration.

Key Point: The AEMC's work on firm standards and LRIC can be used to progress a less ambitious, but highly desirable, form of generator access to transmission.

Future steps – limited access settlement

As well as a level of recognition in the planning domain, Alinta Energy is still particularly interested in inter-regional firmness and sees this as one of OFA's possible major benefits. Unfortunately, under the existing proposal the conceptual benefits are unlikely to arise as inter-connectors have been effectively allocated zero rights.

Alinta Energy is interested in the AEMC considering if access settlement was not generally adopted across the National Energy Market, whether it could be progressed in a form for the purpose of firming inter-regional settlement residues only.

Under this approach, the purchase of access rights over the inter-connector which has a known measureable capacity would create a financial right. This right would be different to the intra-regional rights that exist only in the planning domain against which settlement would not be adjusted in the face of intra-regional constraints.

Alinta Energy appreciates this issue requires further consideration but notes that improved inter-regional competition is seen as one of the major benefits of OFA, and one that is not wholly dependent on management of intra-regional constraints, but that has been largely parked in the current OFA discussions.

National Energy Market wide access settlement

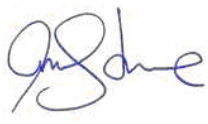
As clearly enunciated, the case for National Energy Market wide access settlement has been dealt a severe blow by the work of the Australian Energy Market Operator. Hence, for Alinta Energy, an alternative scaled back version of OFA remains desirable. Notably, if a less controversial and less complex version of OFA were progressed to implementation it may allow for reconsideration of across the board access settlement in the more distant future (i.e. reassessment in 5 years' time).

Importantly, should market conditions evolve such that congestion became more significant or distortive, the case for implementation can be progressed at an earlier stage. That revisitation relies upon further modelling to identify access settlement impacts or alternatively a trial, should one be possible.

In any case, the conclusion that access settlement should be the one of the last, and not the first, components of the OFA that should be considered for implementation, as suggested by Alinta Energy as far back as 2012, is becoming more apparent.

If you have any queries in relation to this submission please do not hesitate to contact me on, telephone, (03) 9372 2633

Yours sincerely,



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