

18 September 2009



Dr John Tamblyn, Chair
Australian Energy Markets Commission
PO Box A2449
Sydney South NSW 1235

Dear Dr Tamblyn,

ERC0094: Improved RERT Flexibility and Short-notice Reserve Contracts

The Energy Users Association of Australia (EUAA) is a non-profit organisation focused entirely on energy issues with membership exceeding 100 organisations. Our members' energy usage accounts for a significant proportion of Australia's industrial consumption of electricity and gas, and energy costs make up a significant part of their operating costs. The EUAA was formed in 1996 and has represented its members' interests in energy policy and regulatory issues, energy reform, network pricing reviews and climate change issues.

This submission provides some brief comments on this rule change proposed by the Reliability Panel (Panel). The EUAA opposes the rule change because the Reliability Panel has not made the case that this approach is the best way to address the problems it is meant to address.

- The proposal comes from an original MCE reference following the range of interruptions to electricity supply in South Australia and Victoria in January 2009. These interruptions were of serious concern to the EUAA and its members. Our own internal assessment led us to believe that they raise a range of serious questions about the ability of the National Electricity Market (NEM) to deliver the security and reliability users expect from the NEM. We look forward to the various reviews by the AEMC and the Panel reviews looking at this issue.
- As the Panel comments in its Rule Change Proposal, these interruptions were not just reliability incidents but also involved "...a system security incident that resulted in involuntary load shedding ...(and)... a number of distribution system failures interrupting customers"¹ and so are concerned with issues that are partly outside the Panel's authority.
- These interruptions occurred after the amendments that saw the Reserve Trader become the Reliability and Emergency Reserve Trader (RERT) in 2008. The RERT was designed to improve upon the previous mechanism's ability to meet potential reliability shortfalls. Yet it did not prevent the reliability related events of January 2009 and it was never designed to address the security and distribution related interruptions.
- So after one year of the RERT, further changes are proposed that, if implemented, will only address a small part of the January 2009 problem and the more fundamental questions about the market that it raises. While the Panel may claim that the rule

¹<http://www.aemc.gov.au/Media/docs/Reliability%20Panel%20Rule%20change%20proposal-708cd1c6-a16d-450f-864c-2490fae80ba-0.pdf> p.vi

change will bring "...possible improvements to the management of security events"², it would be pure luck if the capacity secured as part of the revised RERT were on the right side geographically of a security event.

- You would be aware that the Reserve Trader was originally introduced as a temporary mechanism at the start of the NEM in 1998 because it was felt that the energy only market needed some transitional support while it developed and matured. Sunset clauses were introduced because of the said temporary nature of the arrangements. There were fears that the NEM could fail to deliver sufficient capacity once the excess supply that characterised large sections of the market reduced and this reduction in reserve capacity could result in unacceptable price volatility given the \$5,000 VOLL that applied at the time.
- However, numerous sunset dates have come and gone in the intervening decade with repeated extensions granted. Based on this past experience, there is every reason to believe that this will be further extended beyond the current sunset on 30 June 2012, particularly if there is nervousness over the impact of Carbon Pollution Reduction Scheme (CPRS) and 20% Renewable Energy Target (RET) on reliability.
- The Panel acknowledges in the Rule Change Proposal³ that RERT (and presumably Reserve Trader before it) is a market distortion. We concur with this view.
- Yet for all the effort put into it, our understanding is that it has only been used to contract capacity on a few occasions and even then the contracted capacity has never actually been dispatched. We are aware that on the last such occasion, in Victoria in the Summer of 2004/05, the cost to end users was significant. The Panel seems to see this short term capacity reserve mechanism as something that they cannot do without in the long term. Like a safety blanket it is "nice to have in case you need it". As long as it is there, if there is an incident like January 2009, the AEMC and NEMMCO can point to the fact that RERT was in place, even if it had no impact. This is seen as preferable to a situation where there was no RERT and exactly the same events in January 2009 occurred.
- It seems that the Panel believes that the energy only market has not yet grown up and matured and we need to retain the capacity reserve blanket in the long term, irrespective of its added value, costs and inefficiencies. Yet the AEMC seems to be happy that the MPC/VoLL and CPT mechanisms do not require any medium term capacity reserve blanket mechanism to address the risk from CPRS and 20% RET⁴.
- On the current rule change proposal, the Panel argues that "...prudent incremental improvements... are warranted to further increase flexibility... ." This seems a strange position to take given the supposed temporary nature of the mechanism and an alternative view would suggest that it is simply a further distortion on top of an existing one.
- The Panel supports these "...prudent incremental improvements" by saying it will have the same sunset clause as the existing RERT, but the EUAA believes that history suggests that probability of the sunset clause actually applying is remote.

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<http://www.aemc.gov.au/Media/docs/Reliability%20Panel%20Rule%20change%20proposal-708cd1c6-a16d-450f-864c-2490faae80ba-0.pdf> p.x

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<http://www.aemc.gov.au/Media/docs/Reliability%20Panel%20Rule%20change%20proposal-708cd1c6-a16d-450f-864c-2490faae80ba-0.pdf> pp.vii and ix

⁴ <http://www.aemc.gov.au/Media/docs/Second%20Interim%20Report-5b4f2d74-8c01-4546-8805-c992d196e35f-0.PDF>

- Being “incremental” and “administrative” leads the Panel to argue⁵ that there is no need for “...a detailed cost-benefit analysis”. The EUAA finds this difficult to believe given the concerns raised by the NGF and ERAA in their submission⁶ on the expedited process.
- The EUAA is concerned that the haste to put this proposal in place has meant that there has been insufficient consideration of these costs.
- It leads us to wonder what “incremental” and “administrative” change the Panel will propose if this revised RERT is implemented and problems persist in the 2009/10 summer. Will we see yet another call by the MCE for action and yet another RERT variation? A distortion on a distortion on a distortion? When will this incremental approach end? It leaves market participants and end users with a considerable level of regulatory uncertainty and is not consistent with the objective of evidence based good regulatory practice. The cost burden of this regulatory uncertainty falls on all consumers.
- This incremental approach also may give the impression to the market that the Panel is unable to appropriately consider reliability issues in a long term framework. It will simply continue to tweak the existing mechanisms at regular intervals, and claim that the changes are “predominately administrative in nature”.
- This continual incremental approach to reliability settings also suggests that there may be something more fundamentally wrong with the reliability mechanisms. However, this question and the fundamental issues that arise about the design of the NEM have never been fully or adequately explored by anybody in decision-making capacities. This is becoming a major concern for energy users.

In summary, the EUAA does not support the Panel’s view in the Rule Change Proposal⁷:

“...that these efficiency improvements are likely to promote the long term interest of consumers of electricity through improved reliability of supply and possible improvements to the management of security events.”

The approach of the Panel and the AEMC to the Rule Change means that it is highly unlikely to meet the National Electricity Objective. The lack of a comprehensive cost-benefit analysis and the regulatory uncertainty created by the proposal adds to the concerns.

We are aware that we are not the only stakeholder raising concerns about this proposal. The submission from the NGF and ERAA also raises concerns about the impact of the proposed changes on generator behaviour that may have the effect of raising electricity prices to consumers. We particularly support the following points from the NGF and ERAA’s submission:

- The ST RERT represents a distortion to the market and will not prevent the type of load shedding events that prompted its proposal.
- The ST RERT purports to incentivise demand side response, which the initial market design was designed to promote. This implies a more fundamental problem with the NEM that needs to be addressed.

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<http://www.aemc.gov.au/Media/docs/Reliability%20Panel%20Rule%20change%20proposal-708cd1c6-a16d-450f-864c-2490faae80ba-0.pdf>

⁶ <http://www.aemc.gov.au/Media/docs/NGF%20and%20ERAA%20objection-ac455613-5145-49ca-a112-8902bf5f8ac4-0.pdf>

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<http://www.aemc.gov.au/Media/docs/Reliability%20Panel%20Rule%20change%20proposal-708cd1c6-a16d-450f-864c-2490faae80ba-0.pdf>

- The Reliability Panel have not made a case that the proposal advances the NEM Objective as a comprehensive cost/benefit analysis has not been done.
- The proposed Rule Change increases regulatory uncertainty since it indicates a culture of ongoing *ad-hoc* changes to the Rules.

The EUAA looks forward to the output of the Panel's forthcoming "Reliability Standards and Setting Review". The EUAA believes that the interests of all consumers would be better served by a more fundamental review of the reliability mechanisms and related aspects of the NEM.

Yours sincerely

A handwritten signature in black ink, appearing to read "Roman Domanski", with a stylized flourish at the end.

Roman Domanski
Executive Director