



3 February 2012

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

Dear Mr Pierce,

Draft Rule Determination – National Electricity Amendment (Expiry of the Reliability and Emergency Reserve Trader (RERT)) Rule 2012 - ERC0132

AGL Energy Ltd. (AGL) welcomes the opportunity to respond to the National Electricity Amendment (Expiry of the Reliability and Emergency Reserve Trader (RERT)) Rule 2012 - ERC0132

AGL operates across the supply chain and has investments in coal-fired, gas-fired, renewable and embedded electricity generation and electricity retailing. AGL is Australia's largest private owner, operator and developer of renewable generation in Australia and has invested well over \$2 billion in renewable energy and has much more in its portfolio of development opportunities. Within the next few years, AGL will own or operate approximately 1,420 MW of renewable energy generation assets.

AGL supports and is a party to the submissions on this matter made by the Private Generators Group and the ERAA. As these submissions note, the RERT (and previously the Reserve Trader) has not increased actual supply reliability in 10 years. We also contend that the deficiencies with the arrangement are well documented. AGL therefore maintains its strong position that the RERT:

- Is clearly ineffective in providing reserves to meet supply shortfalls. The reserve contracts entered into in 2005 & 2006 provided only 84 MW and 374 MW for the South Australian and Victorian regions and AEMO did not receive a single expression of interest in response to its most recent RERT Panel request¹. As AGL has stated in past reviews of the RERT, we have found that most of the reserves provided by this process are scavenged from existing demand side response normally available to retailers.
- Creates a secondary market, outside the primary market, which distorts supply and demand signals and contradicts the AEMC principle of "allowing energy markets to operate without distortion as the primary means of protecting the interests of consumers"².
- Is an unnecessary cost burden borne by both industry and consumers at a time when energy prices are rising and inefficiencies in energy costs are being highly scrutinised. Since its introduction AEMO (NEMMCO) has only ever entered into reserve contracts in 2005 & 2006 at an estimated cost of \$5.4 million, exclusive of administrative costs, paid for by the industry and consumers – for little or no benefit.

¹ Australian Energy Market Operator, AEMO Communication No. 876 – NEM – Update on the Request for Expressions of Interest for RERT Panel, e-mail, 30 November 2011.

² Australian Energy Market Commission, *Draft Rule Determination, National Electricity Amendment (Expiry of the Reliability and Emergency Reserve Trader) Rule 2012*, December 2011

We note that any form of reserve trading which operates outside the primary market will have these distortionary impacts and unnecessary cost burdens.

AGL also provides the following comments in relation to the submissions made by the Victorian Department of Primary Industries and the South Australian Department for Transport, Energy and Infrastructure and the report by Intelligent Energy Systems (IES) which forms part of the latter submission. The IES report is titled "Review of the reliability and security in the absence of the RERT".

AGL understands that the Commission draft decision to extend the RERT was based on the views expressed in these submissions that market uncertainties and the low Market Price Cap necessitated its retention.

The IES report does not appear to provide any comment on whether or not the RERT would be adequate to address any potential shortfalls in supply; rather it is a review of the methodology and assumptions made in the ROAM report which was the basis for establishing the current reliability settings including the MPC. The IES report questions the validity of the results on which the settings are based. IES summarised their conclusions as follows;

"IES undertook its own modelling for the purpose of verifying the modelling undertaken by ROAM and for investigation of factors not considered in the AEMC and ROAM reports. This incorporated the impact of load and wind generation uncertainty and the dynamics of the spot market in terms of generator entry and generator bidding. This analysis and modelling showed the following:

- *That the MPC v USE relationship presented by ROAM can be closely reproduced through simple spreadsheet analysis, reflecting that this relationship largely represents the assumed pattern of load (net of the assumed wind generation) and the number of hours the marginal OCGT plant is required to operate at a price near the MPC to be economic.*
- *There is evidence to suggest that a full incorporation of load and wind uncertainty would result in a significantly higher estimated value for the MPC required for extreme peaking plant to be economic;*
- *The dynamics of actual capacity investment observable in the market to date do not match the approach used in the ROAM modelling. This is especially true for OCGT plant;*
- *The spot price outcomes and new entry economics show considerable variability on an annual basis due to uncertainties in demand and other stochastic factors;*
- *Including the AEMO constraint equations in the modelling results in a near doubling of the expect level of USE. Given that these equations understate the constraints that would actually be expected and that they combine both intra-regional and inter-regional issues, the matter of transmission needs to be more fully understood."³*

In summary it would appear that in the ROAM modelling it is highly likely that the MPC has been understated⁴ because;

- the occurrence of maximum demand has been overstated, consequently generator revenue has been increased,
- the impact of constraints has been understated,
- the use of fixed loads and wind patterns has reduced the uncertainty of outcomes.

The contention from SA is that, based on the limitations of the modelling identified by IES, significant increases in USE are possible in the future with the current reliability settings, particularly in SA. This may be true, but:

- because history has shown that the amount of additional reserve available through the reserve process is small (even assuming that all that all the capacity contracted would otherwise not be available); and
- whilst we appreciate that the Commission is concerned about protecting the key objectives of electricity services in the NEM, it would be unwise for the Commission to be relying on the RERT to address any market deficiencies that result from the current settings of MPC and CPT;

retention of the RERT is an inappropriate remedy. The correct approach would be to refer that matter back to the Reliability Panel for their review.

³ IES Review of the reliability and security in the absence of the RERT – A report to the Department for Transport, Energy and Infrastructure South Australia, page vi.

⁴ "In undertaking their analysis, ROAM did not appear to properly account for the full distribution of load and wind generation. An analysis of the MPC needed for a "last peaker" to be economic in South Australia showed a required MPC of near \$40,000/MWh". IES Report page iv.



The remaining uncertainties regarding future market outcomes outlined in both the Victorian and South Australian jurisdictional submissions appear to relate to:

- the implementation of a carbon price and associated phased closure of affected plant (which should be implemented in a manner to ensure system reliability is maintained), and
- the implementation of the LRET, (to the extent it has been appropriately represented in the market modelling)

Neither of these uncertainties are addressed by a RERT style of mechanism, a matter which was dealt with in earlier submissions.

AGL therefore contends that retention of the RERT beyond the currently scheduled end date is unjustified. We would therefore urge the Commission to make no rule and allow the RERT to finally pass into history.

If you have any questions regarding this submission please contact Roger Oakley on 0386336217.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Alex Cruickshank', is positioned below the text 'Yours sincerely,'.

Alex Cruickshank
Head of Energy Regulation