30 April 2015

John Pierce
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Lodged electronically via: http://www.aemc.gov.au
Reference: EPR0039

Dear Mr Pierce

Stanwell Corporation Limited (Stanwell) welcomes the opportunity to respond to the Optional Firm Access (OFA) Draft Report. The Draft Report concludes that OFA could be an appropriate solution to address the identified issues in the right circumstances, but that market conditions do not currently justify its implementation. Accordingly there is a draft recommendation to monitor market conditions (using an adjunct to the AEMC's existing annual Last Resort Planning Power functions) for indicators of emerging drivers that may justify the implementation of OFA.

The Draft Report's recommendation inappropriately implies that OFA has been developed to a point ready for implementation. Despite all the work undertaken by the AEMC to date, OFA remains many years from being technically ready to implement. There remains enormous unresolved complexity relating to areas such as the pricing model, TNSP incentive scheme, generator "firmness" and coverage of the scheme.

In addition, Stanwell questions key aspects of the "benefit" modelling performed to assess the merits of OFA. It appears that this modelling has been performed on a selective basis, potentially over-valuing the reform. A key example of this is the assumptions of new entrants' required levels of firm access[1], which is at the most OFA-beneficial point derived from previous modelling. This is contrary to the AEMC's consultant's conclusion that generators would be heavily incentivised to hold a high level of firm access[2].

[1] Firm access assumptions for new entrants Wind - 30%, OCGT - 90%, CCGT - 60%, Page 26, Modelling Transmission Frameworks Review, ROAM, http://www.aemc.gov.au/getattachment/271255f4-4323-4931-934d-50566be6be5b/ROAM-Consulting-Modelling-Transmission-Frameworks.aspx

[2] Page 3, Oakley Greenwood, Impact of OFA on Generators, January 2015

Optional Firm Access should never be implemented

Extensive consideration of the proposed design and implementation of Optional Firm Access has convinced Stanwell that OFA will never be the right solution and should therefore never be implemented:

1. ***OFA centralises decision making -*** The pricing model will either drive investment towards or away from a location depending on the assumptions. It is not a neutral party which simply allows the generator to make an 'economic' decision because it fundamentally relies on the future view of a particular entity (whether TNSP, AER, AEMO etc). Stanwell is also concerned that the benefits from OFA rely on the assumption that the complexity of the pricing model will be resolved at a later date without material impact. The current RIT-T arrangement relies on fewer assumptions (such as only a forecast of generation to meet the reliability standard rather than a forecast of all future generation and the level of firm access required) and is conducted through a transparent process.

2. ***Significant locational signals already exist -*** The existing locational signals include marginal loss factors, the risk of constraints in certain network locations and inter-regional price variations. In addition generators have incentives to invest or not invest based on outcomes of the RIT-T.

3. ***There is limited historical evidence of inefficient co-ordination -*** The AEMC have acknowledged "There is limited firm evidence that the current arrangements have caused significant coordination issues to date"[3]. Frontier have also analysed the recent generation investments of Millmerran, Uranquinty and Mortlake and concluded that given what was known at the time, the location of these generators was appropriate[4].

4. ***The network is likely to be bigger -*** Two network standards, the Firm Access Standard and the Reliability Standard can only produce a network that is the same size or greater than one network standard. Given "the majority of generators will be competitively incentivised to hold relatively high levels of OFA"[5], it is likely that the network will be larger rather than the same size.

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[3] Page iii, Transmission Frameworks Review: Final Report, AEMC, April 2013

[4] Page 56, Optional Firm Access design and testing – a response to the AEMC's First Interim Report, Frontier Economics, March 2015, http://www.frontier-economics.com.au/publications/optional-firm-access-design-testing-response-aemcs-first-interim-report/

[5] Page 3, Oakley Greenwood, Impact of OFA on Generators, January 2015

“Highly uncertain” future outcomes are insufficient to warrant fundamental reform

The Draft Report states that should the market undergo “some major shift in market conditions and government settings” or a “major transformation of the generator and transmission capital stock, where the outcomes are highly uncertain” then “the balance of expected benefits and costs of optional firm access would shift in favour of implementation”[6]. Stanwell disagrees with this statement. If market outcomes were so uncertain then OFA will likely lead to worse outcomes than the current arrangements:

1. The OFA pricing model could become even more inaccurate when the future is highly uncertain as the centralised assumptions would be even less likely to represent actual outcomes.

2. These highly uncertain generation investments are unlikely to actually be captured under OFA which applies only to (large) scheduled generators.

3. There are significant concerns as to the robustness of the “benefit” analysis performed to justify OFA. As discussed above, it appears that this modelling has been performed on a selective basis, potentially over-valuing the reform.

Market Monitoring adds to uncertainty

By proposing market monitoring, the AEMC leaves open the possibility that OFA may be implemented in the future. This creates investment uncertainty given the cost and complexity of the reform.

A recent survey of banks performed for the esaa confirms that financing for renewable generation projects is currently unattractive without a long term PPA in place[7]. Under OFA, we expect financiers would also require a firm access agreement in place. While OFA remains possible, this may adversely affect financing rates.

Stanwell has estimated that the cost of firm access agreements to maintain our current level of access is $30m pa - a significant expense in line with Stanwell’s net cost under the Carbon Tax. If market conditions are monitored annually with a view to implement OFA, the risk of this cost burden will continue to remain a concern to participants and financiers.

Participant and financier uncertainty could be relieved if the market were assured that existing investments would receive significant long term transitional access.

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[6] Page i, Optional Firm Access Draft Report, AEMC, March 2015

[7] *State of the Debt Markets for the Energy Supply industry* survey by PwC “… banks would be reluctant to support any new renewable energy projects in Australia unless they were underwritten by guaranteed price contracts…”

http://www.esaa.com.au/media/study_shows_policy_uncertainty_has_stalled_investments_1_1_1_1

If market monitoring were to occur, the conditions would need to be specific and sufficiently indicative of a major NEM-wide problem. Satisfaction of the specific market monitoring criteria should trigger a review into whether a solution is required and if so what the solution could be. If OFA is considered a solution, it would need to be re-evaluated based on its merits at that time. Specific market monitoring conditions could include:

- Evidence of congestion affecting a specified proportion of generators a specified proportion of the time
- The majority of generators are asking for a solution
- Multiple instances of poorly co-optimised new generation and transmission assets in multiple NEM regions over several years. With reference to the Houston Kemp analysis, poorly co-optimised investment which occurred because of inadequate adherence to the existing rules and processes (such as the existing requirement for new generators to not degrade the interconnector) should not be considered a trigger.

Specific targeted reforms (if necessary)

Stanwell supports the AEMC's statement regarding congestion-related bidding or system issues: "Where the materiality of these issues on market outcomes is small and duration likely to be temporary, regulatory interventions are unlikely to be warranted. Where the impact is material, specific and targeted measures can be considered through the rule change process, rather than by changing the foundations of the NEM through optional firm access or market based congestion management systems."[8] Had this view been expressed earlier it may have prevented COAG initiating the detailed design and testing of OFA.

Regulatory burden of ongoing, unnecessary reviews

It is Stanwell's understanding that the AEMC are concerned about the increased centralisation of decision making under OFA as recently published in the Frontier report[9]. This is the same concern that Frontier (and others) raised during the Transmission Frameworks Review: "The greatest drawback of the OFA proposal concerns the methodology for pricing firm access rights. The methodology is extremely complex and abstract… More importantly, the methodology implies a profound centralisation of decision-making power over the planning of, and investment in, new generation and transmission infrastructure compared to the present arrangements."[10]

Stanwell is disappointed that, given the same key concern was known at the time of the Transmissions Frameworks Review, that the OFA work stream was initiated.

[8] Page ii, Optional Firm Access Draft Report, AEMC, March 2015

[9] Page 64, Optional Firm Access design and testing – a response to the AEMC's First Interim Report, Frontier Economics, March 2015, http://www.frontier-economics.com.au/publications/optional-firm-access-design-testing-response-aemcs-first-interim-report/

[10] Page 5, Optional Firm Access, Frontier Economics, October 2012, http://www.aemc.gov.au/getattachment/7bb8fd27-07ec-4775-82b6-25f3ad8dd3df/National-Generators-Forum-Frontier-Economics-attac.aspx

The review of OFA has been costly to the AEMC:

- At least 8 external consultant reports
- Extensive involvement in the design by Creative Energy Consulting
- At least 2 AEMC staff (full time equivalent)
- Input by Board, CEO and senior staff including at the public forum

OFA has also been costly to industry:

- At least 3 industry secondees
- 6 industry working group meetings of 5 hours duration involving 10+ participants. Some must fly interstate to attend the meeting
- 4 industry advisory group meetings involving 10+ participants
- Extensive involvement by AEMO (recovered via participant fees)
- Industry funding of Frontier economics study
- Participants reading, testing and understanding 600+ pages of AEMC reports plus hundreds of pages of consultant reports.
- Responding to submissions

Stanwell estimates involvement in this process has directly cost us approximately $200k. We maintain that the concerns raised and analysis performed during the Transmission Frameworks Review did not support the OFA project, making this a wholly unnecessary cost imposed on Stanwell and other participants, and ultimately consumers.

Stanwell supports the AEMC's statement: "Given the extensive work undertaken on the design and testing of optional firm access, the intent of the Australian Energy Market Commission (AEMC or Commission) is that this will be the last such report for many years to come."[11]

We would welcome the opportunity to discuss any of the matters raised in this submission. Please contact me on (07) 3228 4529 or Jennifer Tarr on (07) 3228 4546.

Yours sincerely

Luke Van Boeckel
Manager Regulatory Strategy

[11] Page i, Optional Firm Access Draft Report, AEMC, March 2015