

# Submission to the AEMC Review of Energy Market Frameworks in light of Climate Change Policies

3<sup>rd</sup> August 2009

Joint submission from Nyrstar Hobart Pty Ltd & Norske Skog Boyer  
Mill

## Modifications to existing Loss Factor methodology

By way of background Nyrstar Hobart smelter and Norske Skog Boyer Mill are two large energy intensive businesses operating near Hobart, Tasmania. Both these businesses make significant socio-economic contributions to Tasmania as well as Australia. These two businesses are negatively affected by Marginal Loss Factors due to their location from the Tasmanian node in George Town. The AEMO's recent determination of Marginal Loss Factors has resulted in 150% and 200% increases in Loss Factors for Nyrstar Hobart and Norske Skog Boyer respectively. This creates a large cost impact that must be absorbed by these operations and cannot be 'passed-through' due to the nature of the global commodity markets they operate in – zinc (Nyrstar) and newsprint (Norske Skog).

There are two issues that are of primary concern to Nyrstar and Norske Skog. Firstly, the large variation in Loss Factors from year to year and secondly the quantum in Loss Factor. The current forward looking methodology employed by the AEMO is deficient as it fails to reconcile Loss factors through the year so that businesses like Nyrstar and Norske Skog could end up paying for a Loss factor that is higher than what actually transpires. The current methodology does not cater for such a situation. Also, despite the AEMO providing reasons why the Loss Factor will be higher this financial year compared to the last the large variation and quantum are problematic on two fronts. Firstly, from a budget risk perspective the final Loss Factor can be higher than what was forecast by these businesses. Secondly, the negative economic impact that results from such a large increase in Loss Factor. The methodology must allow to either cap Loss Factors if they reach some threshold or the impact limited through a 'true-up' mechanism based on regular actual reconciliation through the year. As a comparison businesses near the node pay for no losses and some businesses actually gain through positive Loss Factors. Yet a locational disadvantage is imposed by the Rules on Nyrstar and Norske Skog that existed prior to the Rules being established. This is an inequitable outcome. Furthermore, with a higher MRET target and more deployment of renewables such as wind generation the Southern Tasmanian loss factors are likely to remain high and volatile which adds to the above arguments that the methodology must change.

The AEMC discussion paper refers at page 41 of the second interim report the following,

*“We consider the current framework for setting SLFs annually strikes an appropriate balance between accurate short-term dispatch and long-term locational signals.....*

*However, we welcome views on whether there is merit in developing an insurance product that uses intra-regional residues to finance a tool to help manage the more extreme annual variations in SLF (more than five per cent).”*

Nyrstar and Norske Skog object to the statement that the current framework strikes an appropriate balance. As discussed above the current framework will continue to reinforce a situation of the “*haves and have-nots*”, this affects the competitiveness of those businesses that must absorb a range of costs not only energy related costs. Although the idea of development of a hedge product for Loss Factors is plausible it is hard to conceive whether the market for such products would be liquid enough and then who would be the natural sellers of such hedge products?

In summary, both Nyrstar and Norske Skog urge the AEMC to review the current framework with the view of developing a methodology that minimizes the impact on those businesses that are locationally disadvantaged through Loss Factors. The Loss Factor risk to those businesses is not insignificant and the methodology must be modified to support and not hinder the long-term interests of consumers like Nyrstar Hobart Smelter and Norske Skog Boyer Mill.