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Australian Energy Market Commission
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**Victorian Jurisdictional Derogation – Reliability and Emergency Reserve Trader (RERT) Contracting
Draft rule determination**

Snowy Hydro Limited welcomes the opportunity to comment on matters raised in the Draft rule determination from the Australian Energy Market Commission (the Commission) on the Victorian Jurisdictional Derogation – RERT Contracting.

Snowy Hydro Limited is a producer, supplier, trader and retailer of energy in the National Electricity Market ('NEM') and a leading provider of risk management financial hedge contracts. We are an integrated energy company with more than 5,500 megawatts (MW) of generating capacity. We are one of Australia's largest renewable generators, the third largest generator by capacity and the fourth largest retailer in the NEM through our award-winning retail energy companies - Red Energy and Lumo Energy.

Snowy Hydro is deeply concerned about the distortionary impact of this rule change, the process the Commission followed in arriving at the draft determination and the fact that this rule change is counter to many initiatives the Commission and others have recently been and continue to pursue. All regulatory settings in NEM should be calibrated to incentivise participation in the market. Longer duration contracts for reserves decrease market confidence in operating in the NEM. This is perverse because the ultimate goal should be to encourage participation in the market.

All recent rule changes and initiatives have been aimed at increasing participation in the market and transparency of information. The Retailer Reliability Obligation (RRO) seeks a market response to a forecast supply shortfall while the Commission and the Australian Energy Regulator (AER) also pursue increased transparency in forward markets. The RERT mechanism is non market based and there is a complete lack of transparency in both the tendering phase and also the cost of using the service, which is ultimately borne by customers. It is concerning that the Australian Energy Market Operator (AEMO) will now contract for RERT in a period that has recently been assessed under the RRO to not have a forecast shortage of supply.

The multi-year RERT may cost less than a single year RERT, but it remains more costly than a market based response. It is inequitable that out-of-market generation contracted by the RERT should be entitled to earn revenues based on the value of customer reliability, whereas market participants, who ultimately underwrite security of supply by risking their own capital, are limited to the much lower market price cap.

For the reasons outlined in our original submission, Snowy Hydro continues to oppose the rule change request. As set out below, we believe there are serious long-term costs which have not been properly acknowledged by the Commission. However, to the extent the draft rule is implemented, Snowy Hydro believes that the jurisdictional derogation to the National Electricity Rules (NER) to provide AEMO with the flexibility to enter into multiyear contracts with providers of emergency

reserves in Victoria should be limited to the state of Victoria and not be permanent. In addition we support detailed and frequent reporting requirements to provide transparency and accountability to the market. We consider that this information is vital for an improved understanding of the costs involved with procuring RERT reserves, and explaining the rationale behind dispatching them if the need arises.

The multi-year RERT should not contract beyond the time when the RRO will address reliability issues. Snowy Hydro understand that the Commission will allow AEMO to be able to enter into contracts up until 30 June 2023. Multi-year contracts under the derogation should not extend beyond June 2023 to not duplicate the costs for consumers and disrupt market signals for investment in new permanent market based generation. In addition to the RRO, Victoria already has some form of regulatory mechanism that has allowed AEMO to contract for emergency reserves along with numerous other intervention mechanisms such as Directions and Instructions which could be utilised in cases of genuine market shortfall.

Interaction with the Retailer Reliability Obligation

The RRO will require companies to hold contracts or invest directly in dispatchable energy to meet peak demand, allowing the reliance on the RERT to be materially reduced. It is important that the Procurer of Last Resort remains aligned with the proposed 12-month proposed Enhanced RERT across all NEM states, with no jurisdictional RERT's in the long term. There is no justification to duplicate multiple mechanisms targeted at the same market issues.

The KPMG market congruency report of wholesale market reforms in the NEM for the Australian Energy Council (AEC)¹ clearly noted that there is an inherent overlap between the RERT and the RRO. The RRO works hand-in-hand with the Enhanced RERT to allow AEMO to procure resources a year out from a shortfall. If this further complicated with the jurisdictional RERT which is another related reform then it will lead to inefficient costs to consumers.²

To provide the market with the most efficient outcomes in the long term, AEMO's flexibility to enter into multi-year contracts with providers of emergency reserves in Victoria should be limited to the state of Victoria and must not be permanent. The multi-year RERT should contract up until such a time that the RRO could address reliability issues. In the long-term, the RRO should render the RERT unnecessary and the Commission should give consideration to rolling-back its recent expansion.

Snowy Hydro believes that the Commission should amend the multi-year RERT contracting under the derogation so it cannot occur beyond June 2023. The AEMO term of the multi-year RERT contracts should end to guarantee no overlap with the RRO. The RRO if it is triggered would enable retailers to contract for subsequent periods, which would all be before the latest date for AEMO's RERT contracting of June 2026. Overlapping the processes would just be costly for consumers. Multi-year contracts under the derogation should not extend beyond June 2023.

Transparency

Greater transparency will improve the ability of retailers, consumer groups, governments and policy makers to explain the costs and benefits of emergency reserves to consumers and the industry more broadly, allows efficient investment and operational decisions in response and improves general

¹ KPMG, "Electricity Market Design Principles - Identifying long-term market design principles to support a sustainable energy future for Australia", a report for the Australian Energy Council.

² KPMG, "Electricity Market Design Principles - Identifying long-term market design principles to support a sustainable energy future for Australia", a report for the Australian Energy Council.



market confidence in the RERT process because the market would have greater understanding of the reasons and conditions that required the procurement of the RERT. Snowy Hydro therefore supports the Commission's proposal to enhance information by making AEMO's use of multi-year contracting transparent through:

- identify any contracts that have a term greater than 12 months
- include an explanation of why such contracts were entered into for a term greater than 12 months, including the basis on which AEMO considered the term and volume to be reasonably necessary to ensure the reliability of supply in the Victorian region; and outline the basis on which AEMO had regard to the RERT principles when entering into the multi year contracts
- report on the payments made in respect of each emergency reserve contract (a current requirement on all emergency reserve contracts).³

Snowy Hydro agrees with the Commission that *“the new reporting requirements introduced under the Enhancement to the RERT rule have increased transparency in order to improve market confidence in the RERT process and place an increased level of accountability on AEMO's decision-making.”*⁴ It is vital for the market through the jurisdictional derogation to also have greater transparency around RERT costs which should assist both customers and retailers in understanding the likelihood and the size of RERT costs. AEMO quarterly reports covering both forward looking and backward-looking data, reports within 5 business days of dispatch/activation and a transparent methodology report on how AEMO determined the amount of RERT to procure will provide confidence for the market and full transparency.

Long term cost

The multi-year RERT may cost less than a single year RERT, but it remains more costly than a market based response. The Commission notes that given acquiring emergency reserves under a multi-year contract can lead to lower direct costs for consumers there is a likelihood that the RERT may be needed for the coming few years in Victoria⁵. Snowy Hydro strongly suggests that this only remains a short term fix as interventionist proposals do not portend well for the future of the NEM as a deregulated, decentralised market. Furthermore, any marginal reductions in direct costs are likely to be overwhelmed by the much more significant long-term indirect costs. These costs are not sufficiently recognised by the Commission.

In an energy-only market like the NEM, the spot market serves two equally important functions, firstly, as a short-term energy dispatch and balancing market, and secondly, as a signal for the investment in, and the retention of, generation and storage facilities. Snowy Hydro understand that AEMO would give priority to the first of these functions, however, through the increased intervention it would dismantle the NEM's ability to support efficient decentralised investment in new capacity and the efficient retirement of existing capacity.

The Commission highlights that the expansion of the shadow market will not undermine the efficiency of the NEM, but Snowy Hydro as an operator of and investor in peaking generation strongly believes the RERT adds uncertainty to those investment decisions and that it does undermine efficiency. The sunset period for the derogation, and the application of intervention pricing, mitigate but cannot not resolve the fundamental inconsistency at the heart of this rule change which could lead to expanding a shadow fleet subsidised by out-of-market revenues while

³ AEMC, Enhancement to the Reliability and Emergency Reserve Trader, Rule determination, 2 May 2019

⁴ AEMC, Enhancement to the Reliability and Emergency Reserve Trader, Rule determination, 2 May 2019, pp59

⁵ AEMC, Enhancement to the Reliability and Emergency Reserve Trader, Rule determination, 2 May 2019, pp59

simultaneously hoping that the primary market can support investment in generation through market revenues.

It is also disappointing that the Commission should attempt to ascribe under-investment in new dispatchable capacity to the prospect of Snowy 2.0 in a highly simplified analysis. It then deduces, from the apparent absence of such investment, and from its anecdotal conversations with unnamed 'investors', that the first reason for this lack of investment is the "entry of Snowy 2.0". As AEMO has observed in the *Draft 2020 Integrated System Plan*, between 5-21GW of new dispatchable resources will be needed to firm up the growth of variable renewable generation in the energy transition, far exhausting that able to be supplied by Snowy 2.0. The most likely cause of under-investment is conspicuously absent from the Commission's analysis, namely the uncertainty caused by increased intervention, such as the RERT.

The materiality of potential market distortions and costs created by a multiyear RERT could be significant. Inaccuracy in AEMO demand forecasting have previously unnecessarily triggered the activation of the RERT with the direct cost of the RERT being passed on to consumers. As a consequence, AEMO's RERT is impacting market participants by not earning a return on its investment likely decreasing future investment in new or existing plant. The Commission should not put the market as a second least preferred outcome for the future.

Snowy Hydro appreciates the opportunity to respond to the Draft rule determination and any questions about this submission should be addressed to me by e-mail to panos.priftakis@snowyhydro.com.au.

Yours sincerely,



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