

26/07/2018

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

Dear John

### **ERC0237: Consultation Paper – Enhancement to the Reliability and Emergency Reserve Trader**

TransGrid welcomes the opportunity to provide comments on the Australian Energy Market Commission (AEMC) Consultation Paper on the Enhancement to the Reliability and Emergency Reserve Trader (RERT) rule change.

TransGrid is the operator and manager of the high voltage transmission network connecting electricity generators, distributors and major end users in New South Wales and the Australian Capital Territory. TransGrid's network is also interconnected to Queensland and Victoria, and is instrumental to an electricity system that allows for interstate energy trading.

The AEMC considers it remains appropriate for the National Electricity Market (NEM) to have some form of strategic reserve to act as a safety net and as one of the last resort alternative to involuntary load shedding.

TransGrid supports the need for a strategic reserve in the short run to better enable Australian Energy Market Operator (AEMO) to ensure reliability in the network during the transition period to higher renewable penetration. Given concerns about the risk of potential shortages in supply over the 2018/19 summer, there may be merit in AEMO having additional flexibility in the tools it has at its disposal to ensure that there is adequate supply. However, TransGrid has a number of concerns in relation to the RERT as proposed by AEMO and we do not see this as an optimal policy for the longer term.

TransGrid's main concerns in relation to the enhancement to the RERT proposed by AEMO fall under three main headings, which are discussed further below:

1. RERT contracts may not ensure that electricity is supplied to customers at lowest cost over the long run.
2. The RERT may cause distortions in the energy market, if it provides incentives to participate in the reserve market instead of the wholesale energy market.
3. The use of exclusive procurement practices by AEMO is inefficient, both raising the price and lowering the availability of demand response resources for other parties, such as network service providers (NSPs).

Section 4 provides comments on specific questions raised by the AEMC on the rule change request.

#### **1. RERT contracts may not ensure least cost electricity**

TransGrid is concerned that there is inadequate governance and oversight of the RERT contracting process, with potential for RERT contracts to be established which do not ensure the lowest overall cost of reliable energy to consumers.

Both AEMO and the AEMC have recognised that the potential cost of RERT contracts need to be balanced against the benefits. TransGrid encourages AEMO and the AEMC to consider options to

enhance the governance arrangements for the RERT, in particular to ensure that customers do not pay more for these contracts than their willingness to pay for reliability.

TransGrid supports consideration of a cap on the availability payments that can be offered to reserves. We also support consideration of other options such as the development and use of a 'pre-qualification' panel of reserve providers ahead of time, which could avoid the use of costly contracts a long way in advance, while giving potential reserve providers an indication of the likely need for their services.

More generally, a broadening of the definition of unserved energy in the National Electricity Rules (NER), used by AEMO to inform the market, may result in the need for strategic reserves less often. The current definition of unserved energy in clause 3.9.3C of the NER excludes occurrences from multiple contingency events, protected events and non-credible contingency events. Occurrences similar to load shedding such as voluntary curtailment, mandatory restrictions and large market responses are also not included, even when the effect on consumers is similar to unserved energy.

A broadening of the definition of unserved energy would also better align it with the level of reliability experienced by consumers. For example, on 10 February 2017 the unserved energy in New South Wales, as defined by clause 3.9.3C of the NER, was approximately 290 MWh. However, the actual consumer experience of unserved energy through voluntary curtailment and market or contractual arrangements was significantly higher than this.

## **2. The RERT may cause distortions in the energy market**

AEMO and the AEMC have also recognised the potential for RERT contracts to distort the wholesale energy market, and TransGrid concurs with this concern. The RERT is intended as a last resort mechanism to balance demand and supply, but it could lead to reductions in supply to the wholesale energy market if RERT contracts are more attractive than selling energy via the wholesale market.

TransGrid supports consideration of AEMO's suggestion that limitations be placed on resources transitioning from the energy market to the RERT.

## **3. Exclusive procurement practices are inefficient**

TransGrid is concerned that AEMO's contracting practices under the existing RERT can result in valuable demand response resources being 'quarantined' even if they do not get utilised by AEMO. For example, AEMO's contracts with demand response providers may exclude them from offering demand response to any other parties in the short term. This is more restrictive than the requirements of clause 3.20.3 of the Rules, because it prevents NSPs from accessing those resources for non-market purposes such as network support. This reduces supply and is likely to increase the cost of demand management resources available for network management, for example to projects such as Powering Sydney's Future. Exclusive contracts lock away resources that could be efficiently used elsewhere without threatening their benefits for reliability.

This highlights TransGrid's concern that a lack of co-ordination could lead to inefficient management of reserve, which could lead to higher costs to consumers. Transmission network service providers are well placed to co-ordinate the provision of reserves over their network in order to provide reserves at the lowest cost to consumers over the long term.

## **4. Comments on questions raised by the AEMC**

Question 1 – TransGrid agrees with the AEMC's proposed framework for assessing the rule change request.

Questions 2 and 3 – TransGrid does not support increasing the procurement time and multi-year procurement as the RERT is meant to be an emergency reserve mechanism and not a normal feature of the market. If a capacity mechanism is sought, then the AEMC should consider a capacity market. An increase in procurement time and multi-year procurement would lead to less incentive for market participants to participate in the market. In addition, the RERT is more expensive than market-based solutions.

Question 4 – There should be a focus on the value that consumers place on avoiding high impact and low probability events. This has not been adequately taken into account in the regulatory

framework. The value of customer reliability is an important input into the economic assessment of optimal levels of reliability.

Questions 5 and 6 – The reliability standard only takes into account a limited set of events. As set out above, a broadening of the definition of unserved energy in the NER, used by AEMO to inform the market, may result in the need for strategic reserves less often. The current definition of unserved energy in clause 3.9.3C of the NER excludes occurrences from multiple contingency events, protected events and non-credible contingency events. Occurrences similar to load shedding such as voluntary curtailment, mandatory restrictions and large market responses are also not included, even when the effect on consumers is similar to unserved energy. We do not support tightening of the reliability standard value of 0.0002 of unserved energy. The Reliability Panel is responsible for setting the standard and any changes in reliability metrics should be dealt with outside this rule change by the reliability panel.

Question 7 – TransGrid does not agree with AEMO using the RERT for system security, as there are operational measures to manage system security (which may include load shedding). If there are issues with system security then they should be addressed through power system planning and operation, not through an emergency reserve mechanism which is in place to maintain system reliability.

Question 8 – In principle, we do not agree with the RERT being linked to a different reliability level to the reliability standard, as the reliability standard has been established by the reliability panel.

Question 9 – It is sufficiently complex to work out the procurement volume (the amount that AEMO should procure once it has identified a potential shortfall) in specific circumstances and thus it is not a matter for the NER.

Question 10 – The AEMC identifies three methodologies for determining the volume of reserves. These are: cost minimisation, regret minimisation and value of insurance. The NER could provide flexibility to allow AEMO to use any of the three methodologies as each seems to be a valid approach to valuing benefits to consumers. Value of insurance hasn't been a feature of the regulatory framework. Similarly, regret minimisation hasn't been a feature of the regulatory framework until recently through the Integrated System Plan. However, both of these methodologies have merit as they take into account the value consumers place on avoiding high impact, low probability events. Cost minimisation by itself does not capture the complete value to consumers and a combination of the three would best capture the value consumers place on reliability.

Question 11 – We do not support a framework for standardised products being included in the NER, as it is up to AEMO to determine these in the RERT guidelines. We recommend that the AEMC take care to not be too prescriptive as this would stifle innovation.

Question 14 – We recommend that the AEMC take caution to not be too prescriptive as this would stifle innovation in technologies which can participate in the RERT.

Question 15 – There is a potential for RERT contracts to distort the wholesale energy market, and TransGrid concurs with this concern. The RERT is intended as a last resort mechanism to balance demand and supply, but it could lead to reductions in supply to the wholesale energy market if RERT contracts are more attractive than selling energy via the wholesale market.

Question 16 – Product specifications as outlined in table 6.1 should not be included in the NER. AEMO has RERT guidelines and these specifications are more appropriate to be included in the guidelines.

More generally, we understand that AEMO will be able to access the RERT one year from the forecast reliability gap under the National Energy Guarantee. It is important that the AEMC coordinates with the Energy Security Board to ensure that the RERT and Guarantee are aligned.

## **Conclusion**

In conclusion, TransGrid supports the need for a strategic reserve in the short run. We believe this will provide comfort that AEMO can manage reliability over the short term, however the consultation paper lacks a vision of preferred long term solution that meets the National Energy Objective, and the articulation of the roadmap to realise the vision.

We encourage AEMO and the AEMC to put in place safeguards which limit the cost to consumers of the RERT and which minimise distortions to the energy market. We also encourage AEMO and the AEMC to review AEMO's ability to undertake exclusive procurement practices, which lead to inefficient and costly management of demand management resources in the market as a whole.

If you would like to discuss this submission, please contact Zainab Dirani, Senior Analyst, on 02 9284 3534.

Yours faithfully

A handwritten signature in purple ink that reads "Caroline Taylor". The signature is written in a cursive, flowing style.

Caroline Taylor  
**Acting Executive Manager, Regulation**