AUSTRALIAN ENERGY COUNCIL

Department for Energy and Mining
Government of South Australia
GPO Box 320
ADELAIDE SA 5001

12th December 2018

Submitted via e-mail to: RRO@sa.gov.au

Dear Sir/Madam,

Ministerial Reliability Instrument Amendment Bill Consultation

The Australian Energy Council (the "**Energy Council**") welcomes the opportunity to make a submission in response to the Department for Energy and Mining's *National Electricity (South Australia) (Ministerial Reliability Instrument) Amendment Bill 2019* ("**MRI Bill**").

The Energy Council is the industry body representing 23 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia, sell gas and electricity to over ten million homes and businesses, and are major investors in renewable energy generation.

Discussion

The need for an additional reliability trigger

Under conditions set out in the *National Electricity (South Australia) (Retailer Reliability Obligation) Amendment Bill 2018* ("**the RRO Bill**"), the Australian Energy Regulator may make a reliability instrument which will oblige retailers (and other liable entities) to have qualifying contracts sufficient to meet their individual shares of the one-in-two year peak demand forecast.

The forecasts to which the RRO Bill refers are produced by the Australian Energy Market Operator ("**AEMO**"), pursuant to Clause 4.9.1 of the National Electricity Rules. The consultation paper reproduces Table 1 from the Electricity Statement of Opportunities, highlighting forecast capacity shortfalls in the South Australia/Victorian regions.[1] The Energy Council notes that the consultation paper draws attention to "capacity shortfalls" against a 10% probability of exceedance (i.e. one-in-ten years) demand scenario. This was presented for information in AEMO's forecasting material but is not a measure of the Reliability Standard, which is that Unserved Energy ("**USE**") exceeds 0.002% across a weighted average of all demand scenarios. A weighted average of 0.002% has been repeatedly shown to be close to the optimal economic trade-off of cost versus reliability to customers, and should remain the prime determinant of acceptable reliability. Using only the 10% scenario implies a much more conservative standard than this economic optimum.

The RRO Bill mechanism is intended to only be used on the basis of an exceedance of the Reliability Standard, and its compliance mechanism is directionally consistent, by requiring retailers to be tested against a one-in-two year standard. The more moderate standard in the RRO Bill is totally appropriate in this context, since it provides retailers the flexibility to contract at economically efficient levels. Nevertheless AEMO has broad-ranging energy market operation powers, to ensure reliability and security should conditions deteriorate. These AEMO intervention powers include:

- the Reliability and Emergency Reserve Trader;
- directions; and
- Clause 4.8.9 instructions.

The most recent South Australian Electricity Report[2] confirms that the Reliability Standard is likely to be met for the foreseeable future and, should plans such as the acceleration of projects identified in the Integrated

[1] Australian Energy Market Operator, *2018 Electricity Statement of Opportunities*, August 2018, p.9
[2] Australian Energy Market Operator, *South Australian Electricity Report*, November 2018

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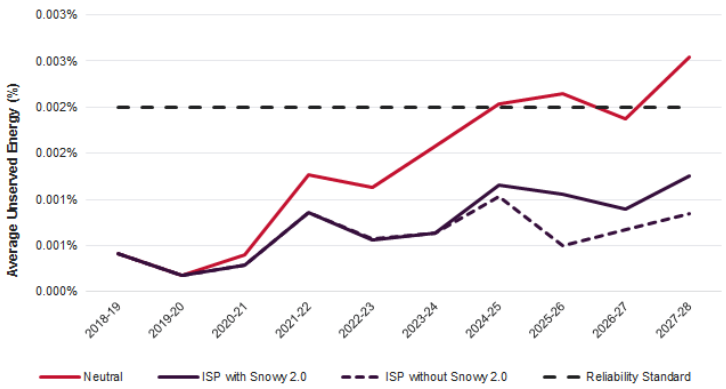
System Plan[3] and the 2,000MW Snowy 2.0[4] project eventuate, there will be no reliability shortfall for the term of AEMO's forecast. This is shown in Figure 27 of the South Australian Electricity Report,[5] and is reproduced below.



On this basis, the Energy Council does not find the case for additional powers to be granted to the Minister to be proven, since there is no expected shortfall against the Reliability Standard.

The consultation paper has conflated the RRO Bill with AEMO's present regular interventions for system strength. These system strength interventions relate to frequently low levels of synchronous generation *unit commitment* at times of low price rather than a lack of installed capacity. There is no reason to expect that a greater level of retailer contracting will in any way change synchronous commitment patterns in periods of high wind and low demand. Fortunately ElectraNet's installations of synchronous condenser equipment are likely to resolve these interventions during 2019.

Minister's ability to make a judgement

The proposed Clause 19B(2) of the MRI Bill sets out the circumstances under which the Minister assesses the need to make a reliability instrument. There are a number of qualitative assessments included in the clause's wording, which cause the Energy Council some disquiet. Specifically, the following words need further consideration:

- "on reasonable grounds" – it is assumed that this assessment can be tested against legal precedent, but if there is an opportunity to better define this term, it should be taken;
- "real risk" – the clause offers no guidance as to how the risk of electricity supply disruption will be assessed as "real". The Energy Council would prefer that the Minister consult with stakeholders to set out guidelines within accompanying regulations which can crystallise when a risk will be defined as "real" and likely to trigger a reliability instrument. Preferably an independent expert should make, or at least guide, this determination;
- "part of South Australia" – the earlier part of the clause considers supply disruption to all of South Australia and this is accepted as a valid metric for assessing risk. However the inclusion of "part of South Australia" necessarily requires a judgement on behalf of the Minister and the Minister's advisers. Taken to an extreme, this could mean the Minister could contemplate making a reliability instrument if a small country town was likely to suffer a disruption;
- "to a significant degree" – again the clause introduces words to qualify the extent of the likely disruption, but the words used are qualitative in nature and require individual judgement to be exercised. To avoid quarrels over when a disruption grows sizeable enough to be "significant", the Energy Council recommends that assessment methods be set out in accompanying regulations and/or the decision is delegated to an independent expert;
- "on 1 or more occasions" – while the expected frequency of supply disruptions is an important consideration, there are other associated criteria which should be considered concurrently, including (but not limited to) the amount of USE and whether the Reliability Standard is forecast to be met. These factors are considered when metrics such as the value of customer reliability are being assessed, and it is important that all factors are included when the MRI Bill's clause is being used.

It can be seen from this preliminary review of the qualitative factors included in the proposed clause that these and many other considerations are critical inputs to any assessment as to whether the exercise of ministerial discretion is warranted. The Energy Council recommends that the legislation include provision for guidelines

[3] Australian Energy Market Operator, *Integrated System Plan*, July 2018
[4] https://www.snowyhydro.com.au/our-scheme/snowy20/
[5] p.56

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to be prepared in consultation with stakeholders, and the assessment criteria set out in those guidelines be as objective as possible.

Minister's ability to truncate the notice period

Under proposed Clause 19B(7), the Minister may make a T-3 reliability instrument 15 months before it takes effect rather than the full three years in advance. This notice period is little more than the T-1 trigger date and the Energy Council believes that truncating it in this way devalues the "double gate" system which was developed in lengthy consultation between the Energy Security Board and stakeholders, and set out in the final detailed design of the National Energy Guarantee.[6]

In the double gate system, a shortfall had to be identified at both T-3 and T-1 before triggering the retail compliance requirement. The justification for this arrangement was that retailers should obtain reasonable notice of any reliability obligation (hence the T-3 notice), but it would be unreasonable to expect retailers to be able to react readily to an isolated T-1 notice, without the benefit of the T-3 warning, particularly as individual T-1 notices may be as a result of *force majeure* events.

With a mere three months' additional notice given by the Minister, retailers will not have sufficient time to procure the additional capacity needed (e.g. by installing a battery system or commissioning peaking generation) to meet the reliability obligation. In addition, despite liable entities monitoring AEMO's Electricity Statement of Opportunities' ("**ESoO**") forecasts as they come closer and closer to the reliability gap year, Year T, the entities may not have entered into the required qualifying contracts when a ministerial instrument is sprung upon them, since their internal forecasts, and indeed the most recent ESoO itself, may have indicated no likely reliability shortfall.

Thus allowing an additional ministerial three month notice period will act to penalise retailers for no improvement in reliability. In addition, the short-term nature of the trigger may unduly affect smaller retailers, who may be unable to react with the speed necessary to meet the obligation, compared with larger retailers with more resources at their disposal. Instead of allowing isolated T-1 triggers, existing last-resort safety-net interventions such as the Reliability and Emergency Reserve Trader should be relied upon to meet any unexpected reliability shortfall.

Market distortion effects

In addition to the fact that the need for the ministerial powers has not been proven, the interventionist nature of granting such latitude to the Minister is inappropriate, and would seriously distort the physical and contractual basis for the National Electricity Market ("**NEM**"). With unfettered powers to make a reliability instrument with as little as 15 months' notice, market participants will be in suspense, awaiting a ministerial determination which may never come. This will affect their planning, purchasing, building and contracting strategies, and will lead to businesses inefficiently allocating capital and expending money to address risks which may never materialise.

Investment confidence arises only when market operational decisions are taken by national institutions separate from governments. The Energy Council therefore opposes these powers on the basis of their distortionary, parochial and interventionist characteristics.

Australian Energy Market Agreement considerations

The Energy Council understands that the Australian Energy Market Agreement[7] ("**AEMA**") governs the operations of the NEM, and that pursuant to Clauses 6.7 and 6.7 of the AEMA, parties to the agreement are compelled to ensure that the Ministerial Council on Energy (now the Council of Australian Governments' Energy Council ("**COAGEC**")) agrees with any proposed amendments or regulations which affect Australian Energy Market Legislation.

It is not stated in the consultation paper, but the Energy Council questions whether the COAGEC has approved the grant of the proposed ministerial powers to an individual jurisdiction. The proposed Clause 19B(3) limits the Minister's power to make a T-3 reliability instrument to the region of the NEM "all or a part of which must be located in South Australia", however with increased interconnection and the ability of regions to be defined

[6] Energy Security Board, *National Energy Guarantee – Final Detailed Design*, 1st August 2018
[7] Australian Energy Market Agreement dated 30th June 2004, as amended from time to time, available at http://www.coagenergycouncil.gov.au/sites/prod.energycouncil/files/publications/documents/Australian%20Energy%20Market%20Agreement%20-%20Dec%202013.pdf

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with respect to transmission assets rather than convenient geographical, state boundaries, there is increased likelihood that regions in the future may be defined which are not limited to South Australia. In this case the exercise of the Minister's powers may affect an adjacent state such as Victoria or New South Wales.

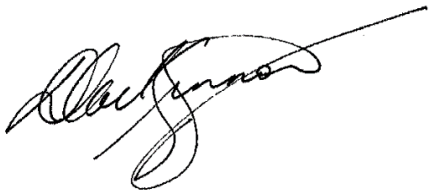
The Energy Council therefore does not believe the limitation expressed in the draft bill is adequate, and seeks assurances that the proposal complies with the AEMA.

Conclusion

In conclusion, the Energy Council believes there are serious shortcomings in the bill as drafted, and the discretion it affords the Minister to intervene in the market with little notice and inadequate justification. It is recommended that further consideration be given to including objective criteria in any risk assessment, and that stakeholders be involved in developing arrangements which can allay any concerns of the South Australian Government that the state's reliability is under threat.

Any questions about this submission should be addressed to the writer, by e-mail to Duncan.MacKinnon@energycouncil.com.au or by telephone on (03) 9205 3103.

Yours sincerely,



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