
# Retailer Reliability Obligation

# Draft Rules Consultation

## Alinta Energy

## Submission

## 5 April 2019

**Submitted via email:** info@esb.org.au

## 1. Introduction

Alinta Energy welcomes the opportunity to provide a submission to the Energy Security Boards' (**ESB**) *Retailer Reliability Obligation Draft Rules Consultation Paper* (the **Consultation Paper**).

Australia's various wholesale and retail energy markets are inherently complex and sophisticated. As such, the ESB faces a significant task in finalising the draft rules to support the implementation of the Retailer Reliability Obligation (**RRO**).

To date, the ESB has thoughtfully and thoroughly engaged with industry in the development of these new obligations and whilst some residual issues remain, the ESB has made exceptional progress in the RRO's design thus far.

To assist the ESB in further refining the Draft Rules, Alinta Energy's views on a number of the RRO design points are outlined below. Alinta Energy recommends that the ESB focus on these areas to further guide and inform the RRO's development.

## 2. Who is Alinta Energy?

Alinta Energy is an active investor in energy markets across Australia with an owned and contracted generation portfolio of over 3,000MW, including 1,700MW of gas-fired generation facilities and 1,070MW of thermal generation facilities. Alinta Energy has a detailed renewable investment strategy across Australia and is pursuing renewable energy projects at an increasing scale. Alinta Energy currently retails electricity and gas to more than 1.1 Million customers including more than 630,000 customers in NEM markets. Alinta Energy is committed to contributing to energy market development across Australia and in all regions as it pursues its growth strategy.

The diversity of Alinta Energy's portfolio, its investment strategy, product offerings, and first-hand experiences across multiple jurisdictions has allowed it to develop a detailed understanding of wholesale electricity markets. Alinta Energy is therefore well placed to provide informed comment in response to the ESB's RRO Consultation Paper.

## 3. Forecasting Risk – Role of the AER

A cornerstone of the RRO is the ability to accurately forecast a "reliability gap", the purpose of which is to provide information to the market about the size of any forecast 'gap' in reserves expressed in terms of MW in a region, at a point in time.

Throughout the RRO's design process Alinta Energy has maintained that in order to prevent governance risks, AEMO's forecasts should be critically reviewed by an independent third party at arm's length. Whilst AEMO is a prudent market operator, AEMO is not a commercial organisation and is not exposed to any of the subsequent costs a triggering of the RRO implies. Any subsequent obligation (and associated costs) are allocated to retailers and ultimately consumers. This should not be seen as any explicit criticism of AEMO per se, rather a critique of the conservative forecasting biases the RRO intrinsically imposes on any organisation charged with undertaking reliability forecasts in this context.

Given this, Industry has been broadly supportive of the AER's independent role in reviewing and authorising the triggering of the RRO, under the assumption that this role would include a thorough analysis and review process that would essentially replicate the forecast modelling to confirm (or not) that the gap indeed exists for the relevant time-period.

As such, Alinta Energy is disappointed that the consultation paper proposes the AER's role to conduct an administrative review only, with the purpose of determining whether AEMO has followed its own forecasting guidelines. Alinta Energy is of the view that this level of scrutiny is inappropriate given the significance a potential forecast gap entails and is not an appropriate governance risk mitigation control.

To prevent scenario's where greater costs are allocated to consumers and /or tax payers than is otherwise required Alinta Energy is of the view that the AER's role should be expanded to independently critically assess or even reproduce AEMO's forecasts. This will minimise forecasting disputes in the future and maximise stakeholder support. Absent such changes, the AER's role is arguably administrative only.

### *4. Procurer of Last Resort*

Alinta Energy notes rule 3.15.9A, gives effect to the socialisation of RERT costs across market customers until participants final compliance positions can be assessed when final revised metering data becomes available (after 30 weeks). Upon a final compliance assessment at 30 weeks AEMO can then recover the accurate level of funds from liable POLR liable entities to recover the RERT costs attributable to those deemed non-compliant at which point reconciliations can be issued.

Alinta Energy is cautious about endorsing such an approach. Firsthand experience indicates that revisions can often be substantial, especially during periods of extreme demand. Smaller or new entrant retailers are likely to be particularly vulnerable to prudential and capital limitations which a 30 week over recovery of significant RERT costs would impose on their business operations until final compliance positions are determined.

An alternative approach would be for AEMO to determine a methodology to estimate RERT costs attributable to those deemed non-compliant earlier with smaller revisions to follow, or to simply apply RERT settlement charges when settlement data is finalised.

### *5. Firmness Methodologies*

Alinta Energy agrees with the broad criteria as set out in rule 4A.E.3 for determining the firmness of standard contracts (strike price, variability profile, likelihood of cover, and other contractual terms which limit the cover).

In relation to bespoke contracts firmness factors, Alinta Energy considers it critical that contracting innovation and the ability for market participants to dynamically manage their portfolio can continue in a manner which does not inadvertently impede or hinder flexible business as usual contracting. To this end, rule (4A.E.5) sets out the default firmness methodology for non-standard qualifying contracts which may be approved by the AER, subject to their firmness guidelines (yet to be published).

Alinta Energy would encourage a warranty provision to be inserted within the rules which would act to ensure that once approved, this firmness factor will not change for the life of the contract. Bespoke contracts are often of long tenure and large volume (for the reason that smaller trades are administratively burdensome to negotiate and transact). As such, participants will want to ensure once approved, the firmness factor will apply to the life of the bespoke contract. Without such a warranty, participants will face ongoing regulatory risks of having contracts revisited frequently across the term, likely stifling contract liquidity in bespoke contracts.

### *6. Market Liquidity Obligation*

Alinta Energy has been participating in the AEMC's ongoing market making arrangement Rule change process, in which considerations of a voluntary market making arrangement for the NEM is being considered. Alinta Energy see's merit in the rule proponent's proposal for the NER to mandate conduct of a voluntary tender process for market making responsibilities in the NEM. The rule proposal is fundamentally preferable to any compulsory market making obligations for the reason that commercial arrangements entered into voluntarily maximise economic welfare and efficiency and also reduce the overall risk profile within the NEM.

Given this rule change's potential interaction with the Market Liquidity Obligation under the RRO, Alinta Energy would encourage the ESB to consider how the establishment of a voluntary market making platform may interact with MLO going forward and the potential consideration of a temporary deferment of the implementation of the MLO rules pending the outcome of the AEMC's current rule change process.

### *7. Voluntary Book Build*

Alinta Energy notes the proposal for AEMO to conduct and operate a voluntary book build platform which would operate as a contract match making platform for market participants in the event of a reliability instrument being made. Since the proposal's inception the idea the voluntary book build platform has received little to no support from industry. A voluntary book build is a role that AEMO is unfamiliar with, and if utilised would be in direct competition with existing market making platform operators such as the ASX. Industry participants have maintained this view throughout the RROs design.

As such, Alinta Energy is concerned with draft rule's proposal (4.A.H.5) to recover book build fee costs from participant fees across the entire market, rather than directly from participants who actually participate in the book build platform. Alinta Energy is of the view that the book build process is unnecessary and unsupported by industry, as such any fees associated from the book build operation should be recovered purely from utilisation charges only directly from participants whom may choose to utilise the service.

### *8. Reserve Contracts*

It is Alinta Energy's view that AEMO's procurement negotiations with reserve contract providers should be strictly limited to the time the reserve contract procurement process is being undertaken only. As such, Alinta Energy suggests that the following wording be removed from clause 3.20.3(f):

*"For the avoidance of doubt, AEMO may negotiate with potential tenderers in relation to reserve contracts at any time."*

Alinta Energy is aware of a growing industry view that AEMO's administration of the recent 2017 - 2018 RERT procurement process led to several large customers choosing to withhold their contracting with existing market participant retailing businesses, in order to contract demand response and other off market generation reserves directly with AEMO for a higher price. AEMO has limited direct incentives to keep the costs of reserve contracts low (as costs are socialised through to the market), the effect of which led to a "crowding out" of commercial market-based options, and a preference to deal with AEMO directly for reserve contract providers.

If AEMO has the ability to negotiate with reserve contract providers at any time, this would ultimately hinder a market-based response to any reliability gap, as providers withhold contracting to the market in the hope of contracting with AEMO (whom they may be in frequent / ongoing negotiations with), conversely driving up costs for the entire market. As such, Alinta Energy is supportive of strict limits being placed on AEMO's ability to negotiate with reserve contract providers being strictly limited to the official reserve procurement process only.

### *9. Reliability Standard*

Alinta Energy supports the view that the reliability standard is the appropriate measure for assessing the economic impact of reliability in the NEM, and as such is the appropriate trigger for the RRO. Nonetheless, Alinta Energy is of the view that a "materiality" tolerance threshold in the reliability standard is necessary within the rules when applied against the RRO to ensure that any forecast breach is indeed material. This buffer is important given the significant costs and compliance activities involved should the RRO be triggered, regardless of the materiality or length of the forecast breach.

Alinta Energy supports the AER within the rules having the discretion to not trigger a reliability instrument when the threshold is reached up to pre-determined level, by considering the costs involved should the RRO be triggered. The AER's discretion should be set within an appropriate tolerance level, which could be assisted with the provision of details and supporting evidence from AEMO's Unserved Energy (USE) modelling, giving the AER the opportunity to critically review AEMO's inputs and assumption data.

### *10. National Electricity (South Australia) (Retailer Reliability Obligation) Amendment Bill 2019*

Under National Electricity (South Australia) (Retailer Reliability Obligation) Amendment Bill 2019, the SA Energy Minister has the ability to make a T-3 reliability instrument if the Minister has the ability to make a T-3 reliability instrument 15 months before it takes effect rather than the full three years in advance, meaning that the Reliability Obligation may be triggered with limited market warning in South Australia.

Whilst outside the scope of the ESB's present consultation, Alinta Energy considers it worth stating that if the South Australian amendment bill is passed as drafted, the amendment would be detrimental to RRO's operation and would likely have the effect of significantly raising risk and compliance costs for participants.

Retailers and other liable entities require prudent notification and time in order to procure additional capacity to meet the compliance requirements as set out under the Reliability Obligation. A 15 month notice period may not allow sufficient time to obtain adequate qualifying contracts to satisfy a material reliability gap should one be identified. In practise, such a shortened notice period would likely act to create a scarcity environment which could act to significantly raise existing contract costs for participants and subsequently consumers.

Alinta Energy does not believe the addition of a shortened notice period is preferable to the original T-3 and T-1 checkpoints. If the proposed changes are warranted, South Australia in conjunction with the ESB should seek Council of Australian Governments consensus. Confusion would ensue if the South Australian Government had powers for a T-3 RRO but the AER maintains sole power to trigger a T-1 RRO.

### *11. Provision of information to AEMO*

To ensure that liable entities can have confidence in the reliability forecast, the ESOO forecasting needs to be based on information that is current and of sufficient quality. To that end, under the draft Rules, Alinta Energy understands that AEMO will have rights (subject to certain limitations) to request information from Registered Participants for the purpose of preparing the ESOO and updates to the ESOO. Information requests issued by AEMO may include:

- Standard information requests via the AEMO portal to all relevant persons.
- Individual information requests to specific Registered Participants, where there is a need to clarify or obtain further information for the purpose of preparing the ESOO.

For example, one such information requirement clause 3.13.3A(g) is currently drafted as:

> *"As soon as practicable after a Scheduled Generator, Semi-Scheduled Generator, Market Participant or Network Service Provider becomes aware of a material change to any information required for publication by AEMO under paragraph (aq), that information must be provided to AEMO by that Scheduled Generator, Semi-Scheduled Generator, Market Participant or Network Service Provider."*

Whilst Alinta Energy understands that the availability of high-quality information to inform the reliability forecast is required for the successful operation of the RRO, Alinta Energy would encourage consideration of inclusions of allowances for operating flexibility. For example, definitions such as "material changes" are broad and once in affect may cause points of contention and debate over what constitutes "materiality". In practise these types of operational occurrences may not be completely certain, i.e. the decision to undertake a long-term outage may require significant analysis to define the appropriate and exact duration. Given this, Alinta Energy suggests that such rules should drafted with reference to more flexible language and tolerable operating allowances. Alternatively, such clauses should not be subject to civil penalty provisions except under specific and clear circumstances.

## *12. Generator Retirement*

The consultation paper raises questions regarding the AEMC's recent Generator three-year notice of closure Rule Change where generators are obliged to provide three years' notice of their expected closure, and the interaction between AEMO's ESOO T-3 forecasting under the RRO. The consultation paper raises the question of whether the existing generator closure notice period should be extended from T-3 years to T-4 to better align with the T-3 Reliability instrument to allow such information to be incorporated into AEMO's forecasts.

Alinta Energy does not support extending the notice of closure for the reason that there are several complexities associated with participants committing to closure dates several years in advance, and these complexities would be magnified under a notice period which extends beyond three years. The further into the future a notice period extends, the more likely confidence in its accuracy would decline given the risk of unforeseen circumstances or changed market conditions.

In any case, in Alinta Energy's view participants are likely to give informal notification of generator closure that would inform AEMO's forecasting. For example, the Liddell generator in NSW has given approximately 8 years notice of closure, absent any rule obligation, such practises are likely to informally continue into the future.

## *13. Conclusion*

To assist the ESB in further refining the Draft Rules, Alinta Energy has raised several design points which may benefit from additional consideration. Alinta Energy recommends that the ESB focus on these areas to further guide and inform the RRO's development.

Alinta Energy looks forward to participating in the ongoing RRO Design process. Please do not hesitate to contact me on 02 9375 0992 or via email anders.sangkuhl@alintaenergy.com.au if you have any queries in relation to this submission.

Yours Sincerely

[Signed]

**Anders Sangkuhl**
Wholesale Regulation Manager