

10 December 2018

Australian Energy Market Commission  
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### **RERT ENHANCEMENT (ERC0237)**

Energy Consumers Australia appreciates the opportunity to comment on the Australian Energy Market Commission's (AEMC) *Enhancement to the Reliability and Emergency Reserve Trader: Options Paper* (the Paper)<sup>1</sup>. This paper forms part of the AEMC's process for considering a rule change proposal made by the Australian Energy Market Operator (AEMO). We have participated in the AEMC's public workshop and have also participated in the Technical Working Group. The views in this submission reflect our contribution in these forums.

Energy Consumers Australia is the national voice for residential and small business energy consumers. Established by the Council of Australian Governments Energy Council in 2015, our objective is to promote the long-term interests of energy consumers with respect to price, quality, reliability, safety and security of supply.

We are concerned about the affordability implications of what is proposed and do not support a change to the RERT framework or the reliability settings at this stage. The experience in the last ten years shows the danger of getting the reliability settings wrong, where network reliability standards were increased in some jurisdictions without enough regard to what that would mean for prices and affordability.<sup>2</sup>

In this submission we provide a snapshot of what consumers are telling us about affordability and reliability, about their willingness to contribute to the reliable and secure operation of the system through demand response, and comment on security and reliability in a transitioning market.

#### *The roles of AEMO and the AEMC*

The AEMC is consulting on a rule change proposed by AEMO. In considering the rule change it is important to understand the different roles and functions of the AEMC and AEMO.

Both the Vertigan review of governance and the Finkel review of future security identified uncertainty about AEMO's role and recommended that the Energy Council issue a statement of role.

In its response to the Vertigan review of Governance COAG Energy Council wrote<sup>3</sup>:

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<sup>1</sup> <https://www.aemc.gov.au/sites/default/files/2018-10/Options%20paper.pdf>

<sup>2</sup> <https://www.accc.gov.au/publications/restoring-electricity-affordability-australias-competitive-advantage>

<sup>3</sup> [http://www.coagenergycouncil.gov.au/sites/prod.energycouncil/files/publications/documents/Review-of-Governance-Arrangements-Response-Table%20-%20January%202016\\_0.pdf](http://www.coagenergycouncil.gov.au/sites/prod.energycouncil/files/publications/documents/Review-of-Governance-Arrangements-Response-Table%20-%20January%202016_0.pdf)



Recommendations	COAG Energy Council response
<p>5.1 That the role of AEMO as the market and systems operator be defined as:</p> <ul style="list-style-type: none"> <li><input type="checkbox"/> facilitating the operation of markets for energy; and</li> <li><input type="checkbox"/> promoting the reliability and efficient operation of energy systems and markets.</li> </ul>	<p>Agree – The COAG Energy Council broadly agrees to Recommendation 5.1. The COAG Energy Council considers that AEMO, as market operator, has a fundamental role to play regarding security of supply issues and that this role should also be acknowledged for in AEMO’s role.</p> <p>The Council agrees that there is a need for more clarity around the role of AEMO in market development. The Council considers that AEMO should continue to have a role in market development given its specific market and system operation roles in electricity and gas. AEMO’s unique role enables it to provide important and strategic insights into market development issues which cannot be provided by other market participants.</p> <p>However, the Council recognises that it is important to ensure there is clarity around how it engages and commissions AEMO to provide advice on market development matters. The Council considers that this clarity can be provided through a clear statement of AEMO’s role (see 5.2 below).</p>
<p>5.2 That the Council issue an AEMO ‘statement of role’ which clearly specifies AEMO’s core role, and includes processes for accessing AEMO’s expertise in market and systems operations and the arrangements under which it is able to undertake other activities.</p>	<p>Agree – The COAG Energy Council agrees to Recommendation 5.2 and tasks SCO to create the AEMO’s Statement of Role in consultation with AEMO.</p> <p>The COAG Energy Council welcomes the opportunity to clarify AEMO’s role through a statement of role</p>

In its response to the Finkel Review the COAG Energy Council wrote:

**Setting the right expectations for energy market institutions**

*By the end of 2017 the Council, in consultation with the ESB, will consider draft Statements of Expectations to the AER and the AEMC, and a Statement of Role to AEMO containing a comprehensive set of outcomes-based performance indicators.<sup>4</sup>*

<sup>4</sup> <http://www.coagenergycouncil.gov.au/publications/report-coag-leaders-finkel-review-implementation>



As far as we are aware these decisions of the Energy Council have not yet been acted on.

In common with the Reliability Panel the above description of the role of AEMO makes no explicit reference to the objectives specified in the national energy laws – in this case the National Electricity Objective (NEO). As a consequence, the functions of promoting reliability and ‘efficient operation’ make no reference to the purpose of doing so, which is captured in the NEO as the promotion of the long-term interests of consumers with respect to price, quality, safety, reliability and security of supply.

This is neither an oversight nor an intentional specification of a different objective, it is a reflection of the fact that AEMO’s functions and powers are subject to the rules, and the AEMC can only make rules that will, or are likely to, contribute to the achievement of the NEO.

We believe that in exercising its rule making powers the AEMC has an obligation to be satisfied that the rule itself contributes to the achievement of the NEO, and also that the construction of the rule ensures that the exercise of delegated authority at all times also contributes to the achievement of the NEO.

We are concerned that some aspects of AEMO’s proposal would result in delegation to AEMO in such a way as to be disconnected from the consideration of the price impact of decisions.

As we have expressed at the workshop and technical working group it is not a sufficient response to concerns about price that the proposal only adds a little to price. The cumulative effect of many such decisions results in unsustainable prices currently being experienced by consumers.

*Affordability is the number one priority for consumers*

To ensure we understand the priorities of consumers we undertake an Energy Consumer Sentiment Survey every six months, with five surveys having now been conducted.<sup>5</sup> The results of the last survey, consistent with the results from the previous four, are that consumers are overall far more satisfied with the reliability of their service than they are with the value for money.<sup>6</sup> The results for each respectively are shown below.

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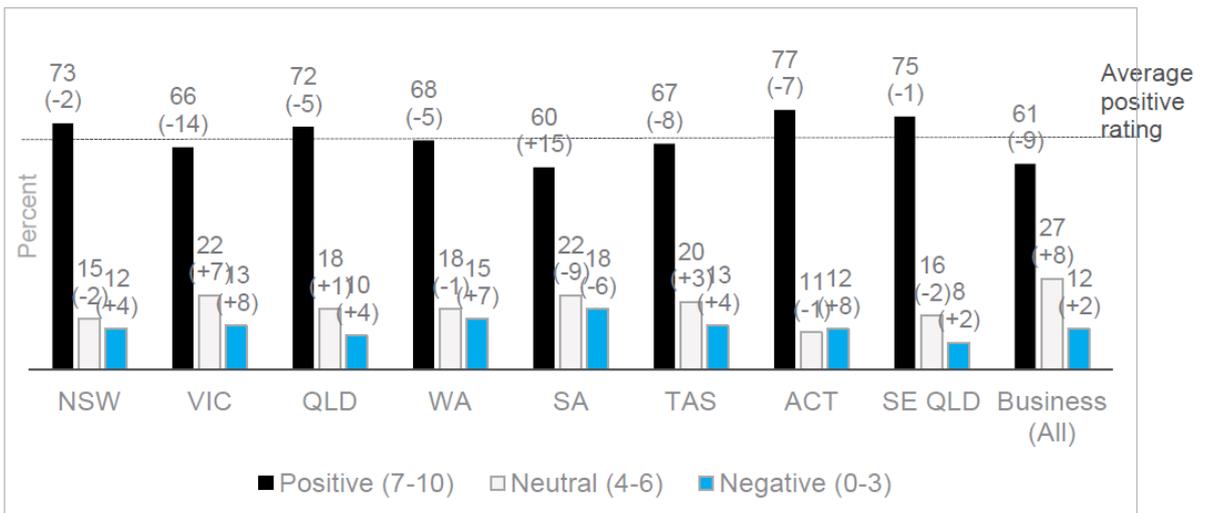
<sup>5</sup> <https://energyconsumersaustralia.com.au/projects/consumer-sentiment-survey/>

<sup>6</sup> <https://energyconsumersaustralia.com.au/wp-content/uploads/Energy-Consumer-Sentiment-Survey-June-2018.pdf>



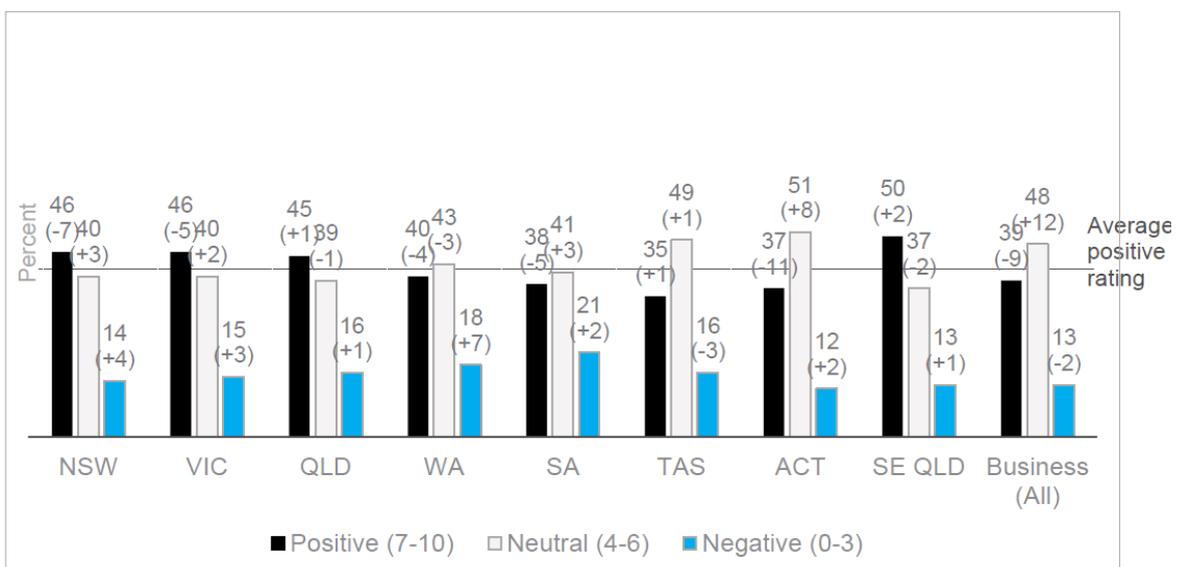
**“Thinking about the reliability of your electricity supply, how satisfied are you with the number of times you’ve had loss of power, blackouts or other faults with your electricity supply in the past 6 months?”**

**0-10 scale, 0=‘not at all satisfied’, 10=‘very satisfied’**



**“How would you rate the overall value for money of the products and services provided by your electricity company in the last 6 months?”**

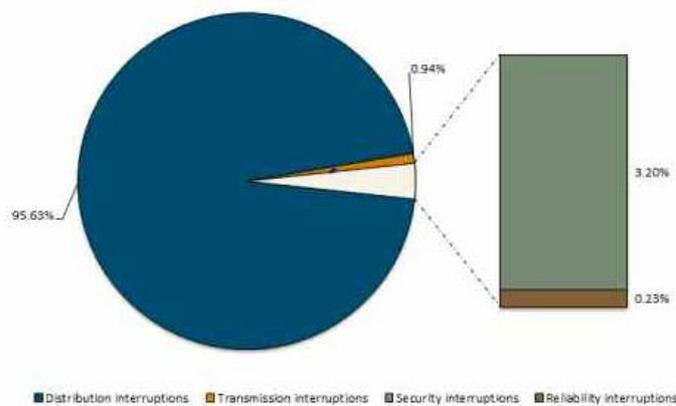
**0-10 scale, 0=‘very poor’, 10=‘excellent’**



Consumers are generally not in a position to identify why their power supply has been interrupted i.e. a network (distribution or transmission) or a generation shortfall). Consequently, the satisfaction level shown above is based on all sources of power interruptions. The AEMC’s analysis (below) shows that only 0.23 percent of power interruptions have been caused by ‘reliability’ issues – where reliability is



defined as the adequacy of generation to supply demand. This is basically the short load shedding in South Australia in February 2017.



Source: Figure 2.1 from the AEMC Reliability Framework Review Final Report <sup>7</sup>

The reported reliability performance of the system in recent times has been heavily influenced by security interruptions – notably the South Australia system black event in September 2016. AEMO has implemented changes to address issues identified in subsequent reviews, including the *Declaration of Lack of Reserve* rule change<sup>8</sup>. While AEMO invoked the long term RERT it acquired last summer on two occasions, we understand that in neither case did a supply inadequacy eventuate.

#### *Markets preferred to interventions*

We acknowledge that there is a public debate about the reliability of the system. However, the evidence indicates that there are adequate generation resources. There are system security concerns and ‘resilience’ concerns, but these are not consequences of resource inadequacy.

This is not to say that a transitioning fuel mix does not bring with it challenges around maintaining reliability. The variable output of many renewable generation sources makes matching supply and demand more challenging, however this is not a new problem. Large thermal power plants tend to work best when producing a consistent output and the challenge historically has been to find ‘base load’ demand to utilize this energy. This was the motivation for the development of off-peak hot water – a load that is only slowly being moved to match the availability of generation.

One of the intended benefits of electricity market reform was the development of ‘greater demand management and a less “peaky” demand curve.’<sup>9</sup> Today the objective is not so much less peaky demand, but demand that can be aligned with available supply.

In the Paper the AEMC notes that it will consider ‘minimising market distortions’ in its assessment of the rule proposal. We support this consideration, but in doing so note that the reason for doing so is that the consequence of market distortions is that consumers pay more than they need to. Market distortions are typically very costly to consumers.

<sup>7</sup> [https://www.aemc.gov.au/sites/default/files/2018-07/Final%20report\\_0.pdf](https://www.aemc.gov.au/sites/default/files/2018-07/Final%20report_0.pdf)

<sup>8</sup> <https://www.aemc.gov.au/rule-changes/declaration-of-lack-of-reserve-conditions>

<sup>9</sup> From the benefits of reform listed in the Victorian Treasury’s *Reforming Victoria’s Electricity Industry* December 1994 P.6)



The challenge for any regulator designing a market mechanism is that the market cannot be relied upon to provide either appropriate consumer protections or efficient investment until it has developed. The market designer has to consider in their design rules how best to encourage the development of the market to overcome this deficiency.

It is easy to make the mistake that the limiting the RERT to only contracting for off-market resources results in minimum market distortion. This is not the case, in fact it may amplify the distortion by creating two markets when there only needs to be one. That creates the immediate opportunity for arbitrage between the markets to the detriment of consumers. Intervention mechanisms, of which the RERT is one, should be a last resort.

#### *Determining reliability requirements*

The ultimate question of system reliability – or resource adequacy – is what target should be set for the frequency of involuntary load shedding. It is not feasible or affordable to design a system where there is 100 per cent reliability (no load shedding).

In a market-based system it is assumed that prices will act to balance supply and demand so that involuntary load shedding need not occur. In a market where consumers were exposed to the spot price and had visibility to the price to respond then there would be no involuntary load shedding – load would exit when the price is too high. However, because we do not have such a system, we have instituted a market price cap (MPC) and the value of the price cap is set by reference to how much consumers in aggregate value not having to shed load (the value of customer reliability or VCR).

It is through balancing the expected cost of extra capacity against the value of lost load that the Reliability Panel both determines the MPC and the reliability standard. The standard is derived from consumers' willingness to pay for reliability.

In the Paper (Question 1) the AEMC asks whether “stakeholders agree with our approach as to how the appropriateness of the reliability standard will be considered?” Given that the November workshop has concluded, we are now in a position to answer the related question of whether the reliability standard should be changed for the National Electricity Market or for the application of the RERT. The candidate for a replacement standard is either a Loss of Load Probability or Loss of Load Expectation (LOLP or LOLE). For example, an LOLE that some load would be lost one day in ten years.

AEMO's argument for that change is that the higher variability in the NEM means that the consequence of individual events will be higher – that is that any event will be occurring at a point of high demand and hence will be necessarily catastrophic. This analysis is an advance on historic AEMO analysis that has underestimated the changing supply characteristics, but incorrectly continues to underestimate the responsiveness of the demand side of the market.

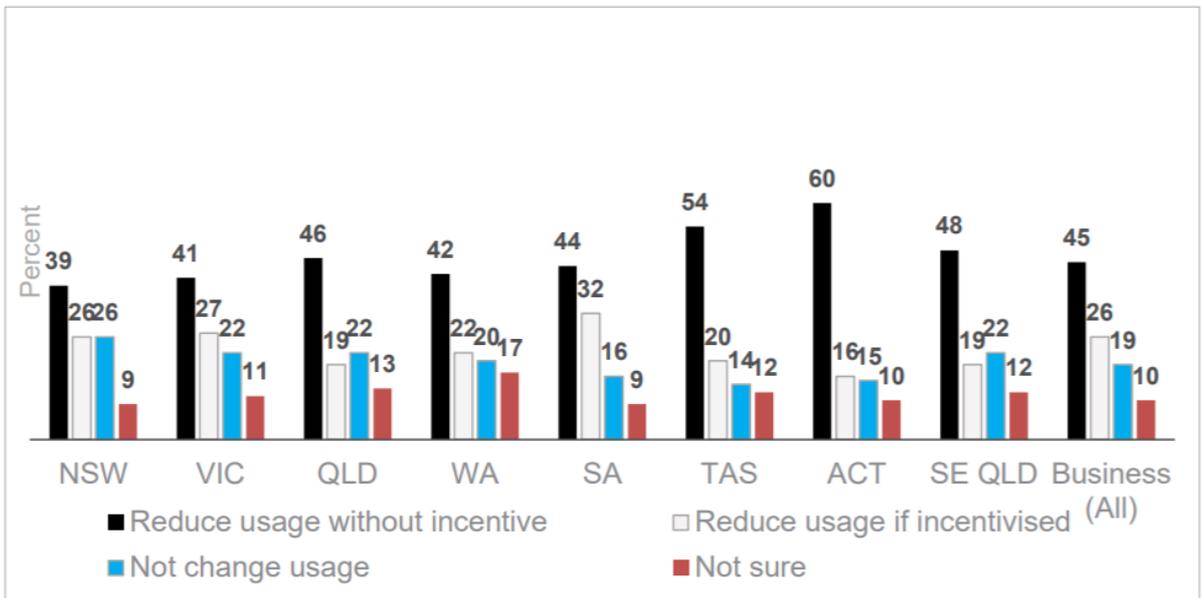
We note in this context that consumers are telling us through the Energy Consumer Sentiment Survey that they are willing to adjust their use to help maintain the security and reliability of the system – many without an incentive, and a significant number with an incentive. These results are supported by the experience in NSW and the ACT in February 2017, where a call by governments for people to adjust their use yielded a significant reduction in demand that helped avoid the need for load shedding.<sup>10</sup>

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<sup>10</sup> [http://www.chiefscientist.nsw.gov.au/data/assets/pdf\\_file/0019/136711/171219-MASTER-NSW-Energy-Security-Taskforce-report-FINAL-SIGNED.pdf](http://www.chiefscientist.nsw.gov.au/data/assets/pdf_file/0019/136711/171219-MASTER-NSW-Energy-Security-Taskforce-report-FINAL-SIGNED.pdf)



***“As you may be aware, sometimes there are campaigns asking people to reduce their energy use during periods of very high demand (e.g. when everyone is using their air conditioning during very hot periods). Such campaigns are often backed by government agencies or respected community groups. If there was such a campaign asking that people reduce their energy use during a very hot period, which of the following would you be most likely to do?”***



Energy Consumers Australia is therefore not convinced the case has made the case for a change in the approach to determining the reliability standard. We are also cautious about comparisons to other markets which typically have far lower MPCs and in many cases also have capacity markets.

#### *Trigger and procurement volumes*

The Paper considers three options for the trigger mechanism and procurement volumes;

1. No change
2. Broader risk assessment
3. Current process with greater clarity

As discussed above we do not see a need at this stage to move away from the reliability standard for any activity that seeks to address resource adequacy in the NEM. We can however see benefit in greater clarity about how this is operationalized. We are also alert to the general case (as expressed in the Governance review, the Finkel review and the ACCC Retail Electricity Prices Inquiry) for the rules framework to be simplified.

It seems to us, therefore, that the process by which greater clarity is provided should be more along the lines of very simple tests in the rules with AEMO being also required to publish its own guidelines on how it operationalises the RERT. That guideline should be subject to its own consultation process and the power of the AEMC to make ‘corrective’ rules should be the discipline provided to ensure the AEMO guidelines are developed in support of the objective.



### *Conclusion*

Energy Consumers Australia approaches the proposed rule change and issues around reliability in a transitioning market with an open mind. Our interest remains ensuring that current and future consumers pay no more than necessary for the quality of electricity services they are prepared to pay for. We are not convinced that there is a need for the changes proposed by AEMO in the operation of the RERT and would prefer to see a focus on growing capability and participation of the demand side of the market.

Should you have any questions regarding this submission please contact David Havyatt, Senior Economist, at [david.havyatt@energyconsumersaustralia.com.au](mailto:david.havyatt@energyconsumersaustralia.com.au) or on 02 9220 5508. Nothing in this submission is confidential and we consent to it being placed on the AEMC website.

Yours sincerely,

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