

Taryn Maroney
AEMO
PO Box 7326
Baulkham Hills BC NSW 2153
By email to SRAS.review@aemo.com.au

Friday 7 June 2013

Dear Taryn,

System Restart Ancillary Services Review – Draft Report

GDF Suez Australian Energy (GDFSAE) appreciates the opportunity to comment on the System Restart Ancillary Services Draft Report (Draft Report). GDFSAE continue to be concerned with the AEMO proposals which would impede the recovery of the power system following a partial or total system black condition. As the market and system operator, electricity consumers are dependent upon AEMO to maintain an adequate insurance against the unlikely but serious risk of extended blackouts. We urge AEMO to re-consider its stated position for the reasons outlined below.

This submission includes a number of general comments in response to the AEMO proposals, as well as some specific responses to identified sections of the Draft Report.

General comments

SRAS objective

The SRAS objective as defined in clause 3.11.4A (a) of the National Electricity Rules is:

"The objective for system restart ancillary services is to minimise the expected economic costs to the market in the long term and in the short term, of a major supply disruption, taking into account the cost of supplying system restart ancillary services, consistent with the national electricity objective".

The primary emphasis of this objective is to minimise the expected costs to the market of a major supply disruption. The objective then states that this primary purpose should be achieved taking into account the costs of SRAS. The SRAS costs are therefore not the primary purpose of the objective, but are something that should be taken account of in seeking to achieve the primary purpose.

The AEMO proposals appear to change the emphasis of the SRAS objective. The AEMO proposals suggest that the primary purpose of the SRAS objective is to minimise the cost of SRAS service. Furthermore, the AEMO proposals suggest that AEMO are willing to impose higher costs onto the market of a major supply disruption, in the interests of minimising the cost of SRAS services.

GDFSAE believe that it is not appropriate for AEMO to interpret the SRAS objective in this manner. If AEMO feel that the emphasis of the objective should be on saving SRAS costs, then GDFSAE suggest that AEMO should seek a Rule change to amend the SRAS objective accordingly.

Low probability event

A system black event is, and has always been, a very low probability event. However, the potential implications of a system black event are so dire, that power system authorities take reasonable steps to be able to recover quickly from a system black event. The fact that there has not been a wide-spread system

GDF SUEZ Australian Energy

Level 33, Rialto South Tower, 525 Collins Street
Melbourne, Victoria 3000, Australia
Tel. +61 3 9617 8400 Fax +61 3 9617 8301

www.gdfsuezau.com

INTERNATIONAL POWER (AUSTRALIA) PTY LTD
ABN 59 092 560 793

black event in Australia's recent history does not mean that such an event cannot occur in the future. The likelihood of a system black event occurring in the future is not influenced by what may or may-not have happened in the past.

Ultimately the provision of system restart capability is an insurance against the unlikely but potentially devastating consequences of a system black event. Although most of us thankfully never suffer the devastation of our houses being destroyed by fire, all prudent house owners still continue to insure their house. In the same way, we should continue to provide the insurance of an adequate system restart capability despite the fact that it has not been called upon to date.

Competitiveness of SRAS market

In table 7 of section 5.2.3 of the Draft Report, AEMO set out what they regard to be characteristics of a competitive market. However GDFSAE suggests that the characteristics identified by AEMO are in fact characteristics of a *perfectly* competitive market.

Wiley 3rd edition of Microeconomics¹ defines a perfectly competitive market as one in which "*Firms are completely free to enter or exit the market...Buyers and sellers have full information about prices...there are large numbers of buyers and sellers*". The same text also notes that "*in the real world, most markets do not have all the features of perfect competition*".

The characteristics identified by AEMO as being indicators of a competitive market are remarkably similar to those identified in the textbook as indicators of a *perfectly* competitive market. It would therefore seem reasonable to conclude that AEMO is confusing the ideal of a perfectly competitive market, with a real world competitive market.

If AEMO believe that an assessment of SRAS market competitiveness is warranted, then a more rigorous analysis would need to be carried out using appropriate metrics. For example, market concentration could be assessed using measures such as the Herfindahl-Hirschman Index or the concentration ratio.

NEM wide versus region black system:

AEMO have suggested reducing the level of system restart capability down from the current NEM wide risk consideration, to one which considers only a regional risk. AEMO have argued that a NEM wide risk consideration is not economically justified, and have also suggested that the NER and SRS support a regional approach.

If AEMO have concluded that a NEM wide approach cannot be economically justified, then it is incumbent upon AEMO to set out in detail, the overall costs and benefits of the current approach and their alternative proposal. Such analysis should include estimates of the total costs of an extended supply disruption. Without such an analysis provided by AEMO, it is not possible to respond in detail to the claim that a NEM wide risk cannot be economically justified.

AEMO also include a statement in section 6.2.1.3 of the Draft Report that it has reviewed the SRS and the NER, and neither specifies a NEM-wide or a region-wide standard. AEMO then suggests that "... it could be argued that no SRAS is required as supply from adjoining areas or regions could be used to restart the affected network".

AEMO should not be inferring anything from the fact that the NER and SRS do not establish the boundaries of the restart standard. The NER and the SRS establish the objectives for system restart, and then ask AEMO to determine the appropriate manner in which to achieve the objectives. It is therefore not informative that the NER and SRS do not specify a NEM-wide or region-wide standard.

From an operational consideration, it is not inconceivable that a system black scenario might involve multiple regions. For example, during hot weather in the southern regions of the NEM, it is quite conceivable that Victoria could be importing power from NSW to the full capability of the NSW-VIC interconnector, and that both Tasmania and South Australia are importing heavily from Victoria. If a catastrophic failure such as an aircraft accident were to damage the NSW-VIC interconnector, it is possible that a voltage collapse situation could occur, which leaves Victoria, South Australia and Tasmania completely shut down. GDFSAE would be

¹ "Microeconomics, 3rd edition" (2006), John Taylor (Stanford), Lionel Frost (Monash), Wiley Publications, Pg 131.

keen to understand how the proposed reduction in SRAS capability would cater with this and other similar scenarios.

The number of SRAS and electrical sub-networks

The studies referred to in appendix 2 of the Issues and Options Paper are difficult to assess, as there is no information provided about the assumptions used, or how the operational complexity and uncertainty of a system restoration has been modelled. AEMO has not provided evidence of the analysis it has completed in support of its proposed amendments. It is therefore difficult to comment on the restoration timeframes indicated.

The draft report seems to suggest that AEMO has already determined that the number of electrical sub-networks and the quantity of SRAS sources can be reduced. However the process for determining the electrical sub-network boundaries and SRAS quantities has not been properly completed and it would therefore seem inappropriate for AEMO to be reaching any conclusions on this.

If AEMO is intending to pursue a reduction in the number of electrical sub-networks and the quantity of SRAS sources, then the Rules require that this be considered through reviews into the electrical sub-network boundaries and SRAS quantities, in accordance with Rules consultation procedures. Such reviews would need to include a more transparent account of the nature of the studies, the assumptions made and the manner in which operational complexity has been included in the studies.

Primary and secondary services definition

GDFSAE has no objection per-se with simplifying the service definitions. However, if AEMO is concerned that the level of competition in provision of SRAS is poor, then eliminating existing secondary service providers will reduce the level of competition even further. AEMO should also take into account that some existing secondary service providers may have incurred costs in establishing and maintaining the ability to provide a secondary SRAS service. If these participants are subsequently unable to offer this service, they will be left with a stranded asset. This represents a form of sovereign risk, which ultimately is also likely to lead to higher SRAS costs.

Procurement arrangements

In section 6.3 of the Draft Report AEMO state that it "... is willing to undertake initiatives to encourage competition in the SRAS market, however is unconvinced that this would have a material impact". It is disappointing that the market operator does not have greater confidence in the benefits that a competitive market can deliver, and GDFSAE hope that this negative view of competition does not interfere with AEMO's independence. As a monopsony purchaser of SRAS, AEMO has an important role in ensuring that SRAS procurement arrangements are competitive.

GDFSAE note that the CS Energy submission to AEMO's Issues and Options Paper included comment on how the threat of new entrants is taken into account when pricing SRAS. CS Energy also noted that there have been very few new entrants into SRAS service provision in recent years. If the AEMO assertion of unreasonably high SRAS costs were true, then it would be reasonable to expect that new SRAS providers would be forthcoming. The fact that new SRAS providers have not emerged runs counter to AEMO's suggestion that SRAS costs are too high.

Adding to the confusion, AEMO respond to CS Energy in their Draft Paper by suggesting that some SRAS offers "... may be priced marginally below new entrant pricing to maximise the return on generator assets..". If AEMO are correct in suggesting that some SRAS offers are being priced below new entrant pricing, surely this is a healthy sign that competition is working, with the threat of new entrants imposing a competitive discipline on SRAS offers.

In response to AEMO retaining the discretion to amend contract details including the contract term, whilst it is reasonable that both parties to any contract negotiation have this right, as the monopsony purchaser of SRAS service, AEMO also has a responsibility to encourage competition through managing the tender process in a transparent and commercial manner. The contract term is a fundamental parameter that needs to be considered by tenderers when deciding on their offer price. GDFSAE therefore believe that it is unreasonable for AEMO to change the contract term after the tenders have been lodged. Such behaviour

undermines the confidence of industry participants in the tender process, and is likely to result in participants either deciding not to participate, or to include a risk premium in any subsequent offer price.

GDFSAE hope that AEMO will consider the points raised in this submission carefully, and approach this matter in a manner which considers the continued effective operation of the NEM, and the ability to respond appropriately to power system emergencies.

Should you wish to discuss any aspect of this submission, please do not hesitate to contact me on 03 9617 8331.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Chris Deague". The signature is fluid and cursive, with a prominent initial "C".

Chris Deague
Senior Market Specialist