



Firm Access Standard & TNSP Incentive Scheme

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Customers will pay more under OFA

Firm Access Standard

- The network is likely to be bigger
- The network is likely to cost more
- Customers still bear the risk of TNSP forecast errors

TNSP Incentive Scheme

- Introduces perverse regulatory incentives

Customers will pay more under OFA: *The network is likely to be bigger*

- 2 network standards under OFA:
 - Reliability Standard
 - Firm Access Standard
- Reliability Standard: paid for by TNSP – passed on through TUOS fees
- Firm Access Standard: paid for by generators – passed on through wholesale prices

Customers will pay more under OFA:
The network is likely to be bigger

Physical size of network
under

**Reliability
Standard**

Customers will pay more under OFA:
The network is likely to be bigger

Physical size of network
under

**Firm Access
Standard**

Customers will pay more under OFA:
The network is likely to be bigger



Customers will pay more under OFA: *The network is likely to be bigger*

- Size of network under 2 standards \geq size of network under 1 standard
- Entire network is the TNSP's Regulatory Asset Base for revenue determinations
- “Over-investment ultimately imposes costs to customers”
- *AEMC, OFA 1st Interim Report, Page 32*

Customers will pay more under OFA: *The network is likely to cost more*

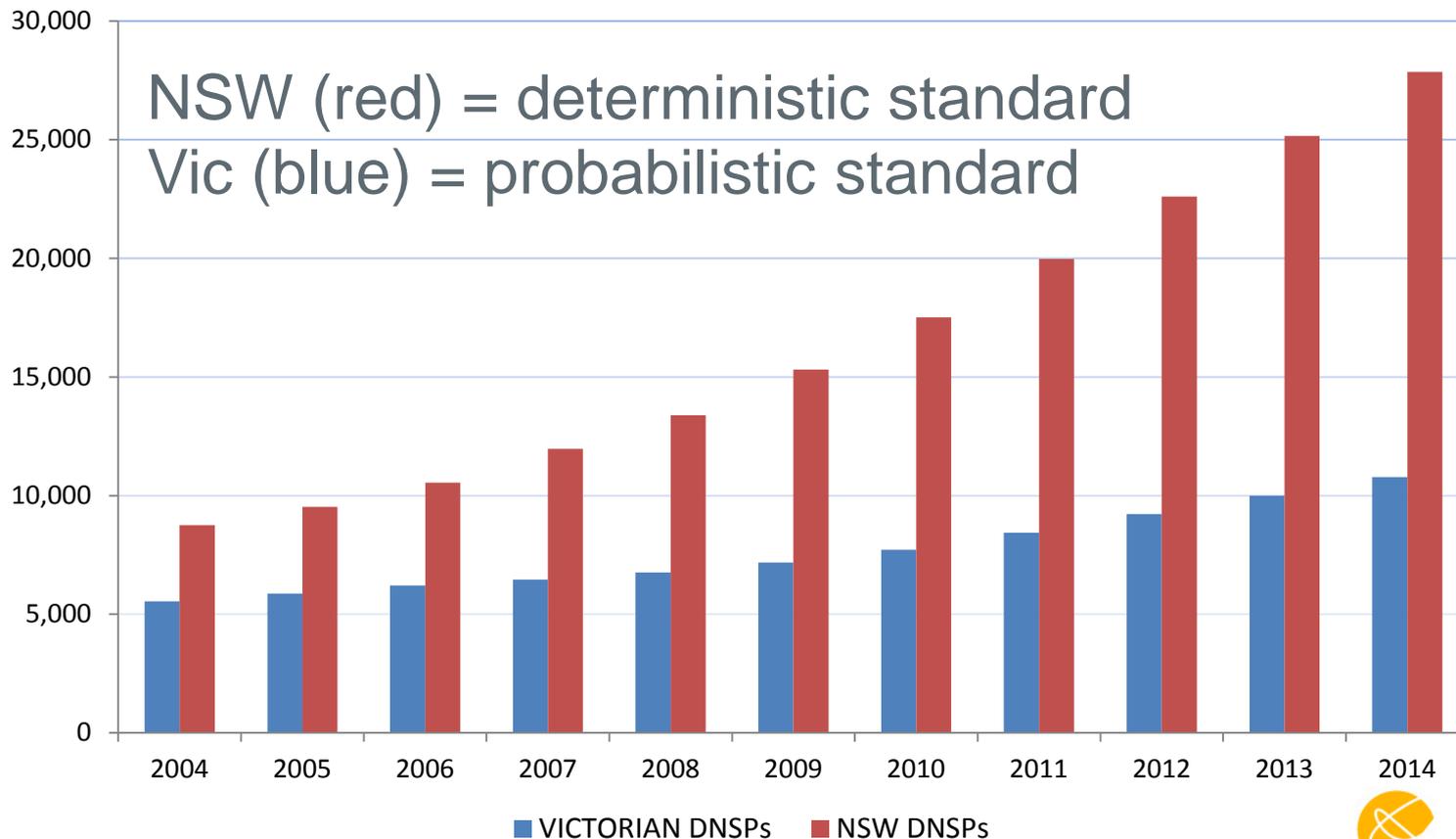
- Firm Access Planning Standard is a deterministic standard
- 2 types of network planning standards:
 - Deterministic: N-1 redundancy
 - Probabilistic: economic cost/benefit
- Deterministic: NSW, Qld, Tas
- Probabilistic: Vic
- Hybrid: SA

Customers will pay more under OFA: *The network is likely to cost more*

- “Shifting away from deterministic standards towards a probabilistic cost–benefit framework **could produce net present value savings in the realm of \$2.2 billion to \$3.8 billion over a 30 year period**”
 - *Productivity Commission Electricity Network Regulation, June 2013 pg 592*

Customers will pay more under OFA: *The network is likely to cost more*

Regulatory Asset Values (nominal \$million)



Source: NSW and Victorian electricity distribution pricing determinations

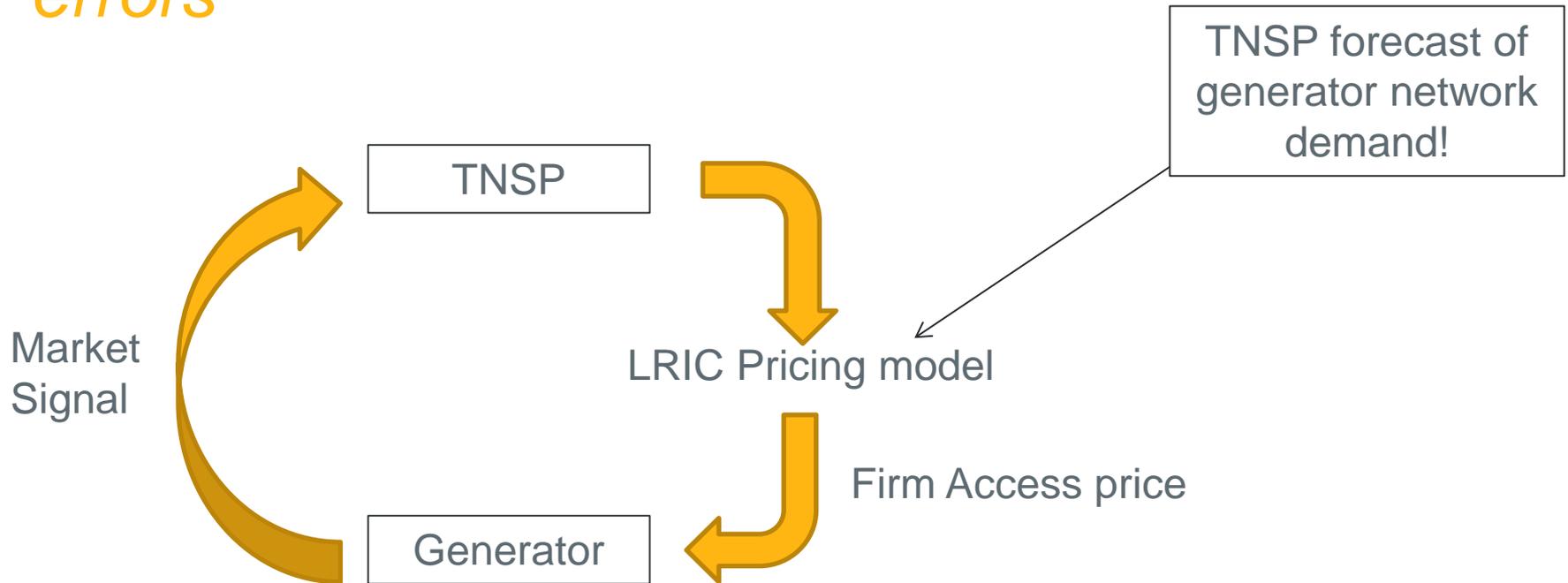
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Customers will pay more under OFA: *Customers still bear the risk of TNSP forecast errors*

- Currently TNSPs forecast generators' future demand for the network
- Customers are exposed to TNSP forecast error

Customers will pay more under OFA: *Customers still bear the risk of TNSP forecast errors*



Customers will pay more under OFA: *Customers still bear the risk of TNSP forecast errors*

- “Under the Long Run Incremental Cost model, existing spare capacity is not generally treated as having zero value because – **even if there are no current bidders for that capacity – there may be bidders in the future. These anticipated bidders are effectively incorporated into the ‘baseline’ assumptions for future demand for firm access”**

- *AEMC 1st Interim report page 81*

Customers will pay more under OFA: *Customers still bear the risk of TNSP forecast errors*

- TNSP forecasting errors lead to firm access price errors *which are ultimately borne by customers*
- “At most the TNSP would be exposed to 100% of the difference between its actual costs and the LRIC estimate, but only until the end of the current regulatory period. **Thus consumers would bear most of the risk of over-runs**”.
 - *FTI Consulting – report to AEMC, April 2013, page 27.*

Customers will pay more under OFA: *TNSP Incentive Scheme will introduce perverse regulatory incentives*

- Regulations and incentive schemes usually lead to unexpected and unintended consequences
- Possible unintended consequences:
 - Schedule as much work concurrent work as possible to minimise TNSP penalties
 - Undersell short term firm access in order to gain incentive payments in the current regulatory period
- Firm Access Planning Standard acknowledged by the AEMC as not enforceable

Conclusion: Customers will pay more under OFA

Firm Access Standard

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Conclusion: Customers will pay more under OFA

“Nothing will bring the reform process unstuck like consumers that have negative experiences”

- *AEMC Chairman John Pierce, ACCC/AER Regulatory Conference, 07 August 2014*

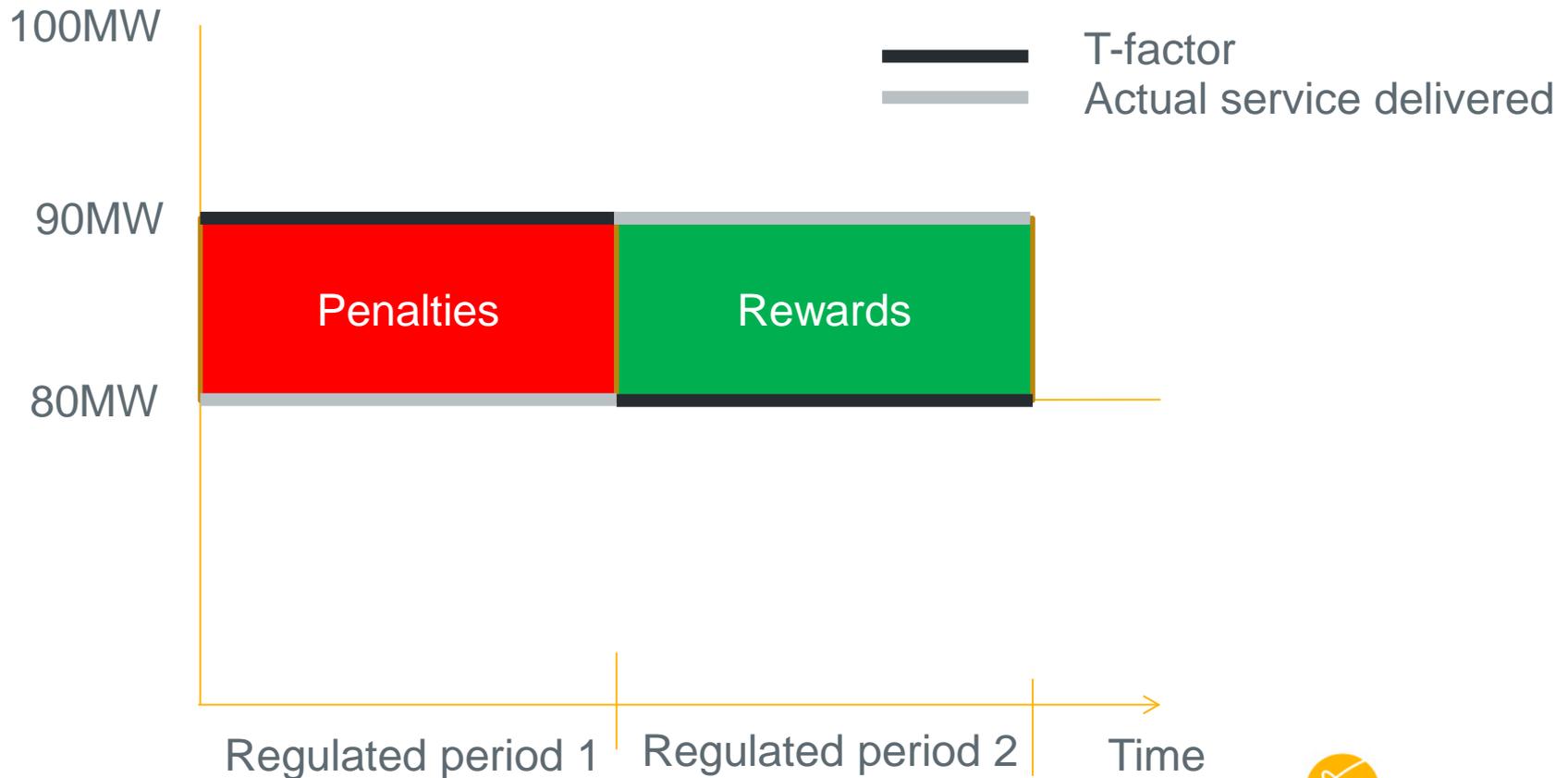
Incentives for disorderly bidding will continue under OFA

- Tarong: Capacity 1400MW, Firm Access 1400MW
- Assume 2 units are put in cold storage: Tarong availability becomes 700MW but capacity remains 1400
- Tarong continues to receive 1400MW Firm Access payments

Incentives for disorderly bidding will continue under OFA

- Total revenue is the sum of:
 - Dispatch payment: $700\text{MW} * (\text{Local Price})$
 - Firm Access Payment: $1400\text{MW} * (\text{RRP} - \text{LP})$
- $= 1400 * (\text{RRP} - \text{LP}) + 700 * \text{LP}$
- $= 1400 * \text{RRP} - \text{LP} * 700$
- Revenue is maximised when the Local Price is minimised.
 - Local price is minimised by disorderly bidding
 - Bidding to \$-1000/MWh maximises Tarong's revenue.

Payments from TNSP Incentive scheme are zero over the long term – assuming T-factor is genuinely representative





thank you

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