NATIONAL GENERATORS FORUM

5 May 2011

Mr John Pierce
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Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Dear Chairman,

National Electricity Amendment (Scale Efficient Network Extensions) Rule 2010 – ERC0100

Introduction

The National Generators Forum (NGF) welcomes the opportunity to make a further submission in response to the Ministerial Council on Energy's (MCE) rule change proposal, entitled National Electricity Amendment (Scale Efficient Network Extensions) Rule 2010 (the Rule Change).

The purpose of this submission is to respond to the Australian Energy Market Commission (AEMC) draft determination.

Our experience as National Electricity Market (NEM) participants with an ongoing interest in the development and governance of the NEM; our direct involvement in the working group formed to consider issues of remote connection as part of the Review of Energy Market Frameworks in light of Climate Change Polices (Market Frameworks Review); and as potential users of any future Scale Efficient Network Extensions (SENEs) informs this submission.

While this submission raises some issues, we continue to support the AEMC's ongoing work focusing on the effectiveness of transmission related services, and at a general level support improved approaches to facilitating transmission investment to meet the needs of customers, existing generators and investors.

More broadly, we commend the AEMC on its extensive consultation.

Organisation Information

The NGF represents the major power generators in the NEM. The installed capacity of the members is 44,384 MW as of 2008, with an asset value of over $40 billion. Annual sales are over 180,000 GWh, valued at around $7 billion. This represents over 95% of the total Australian market.

NGF members are publicly and privately owned businesses which generate electricity for sale and trade under the National Electricity Rules (the rules), and who have registered generating capacity of at least 300 MW. The Chief Executives of these businesses form the Board of National Generators Forum Ltd.

The NGF aims to be a respected industry body recognised for excellence in influencing the development of Australia's energy markets.

Discussion

The NGF sees the AEMC's draft determination as an appropriately structured balance between realising possible scale efficiencies and minimising stranded asset risk. The NGF has a number of comments which are set out below.

Risk allocation arrangements

The NGF supports the AEMC's characterisation of efficient risk allocation in the context of efficient investment decisions. The NGF believes the preferred rule better allocates risk between parties than the original rule change proposal. The original rule change, which required customers to underwrite assets which would be likely to be under-utilised, was considered overly optimistic by the NGF.

In that sense, the preferred rule change ensures market participants or active TNSPs are able to appropriately manage the risk where over investment is likely to be beneficial.

Triggering for considering a SENE

The NGF endorses the process for triggering a SENE and notes it is appropriate that:

- a generator or any other entity be able to trigger a SENE study; and
- a generator not be required to seek a SENE study from a TNSP even though its connection inquiry may be in a location that some parties, including non-market participants, may deem appropriate for possible SENE like assets; and
- the party requesting the study be responsible for arranging its funding to:
    - minimise spurious request;
    - create greater responsiveness between the TNSP and the requesting party to ensure the study meets the requesting parties interests; and
    - provide an indication of other parties interest financially, either additional market participants contributions or the TNSPs own willingness to assist with funding are both indicators of the usefulness of a potential study.

Scope of SENE design and costing study

The NGF endorses the recommended approach to SENE studies including:

- the requirement for TNSPs to undertake sensitivity analysis;
- TNSPs being required to consider a range of relevant matters (see draft determination, p.11) including the most recent NTNDP; and
- publication of the study on the TNSPs website.

The NGF wonders if the absence of propriety rights for the funder of a study may deter an entity(s) from funding SENE studies in some circumstances. This is could be case where a entity may be concerned another party may progress a SENE in advance of its own deliberations.

That being said, the benefits of a SENE in circumstances where multiple connections are highly likely may encourage a consortium of parties to cooperate to connect where the information has been made publicly available.

Trigger for building the SENE

The NGF supports the approach for triggering the building of a SENE. The approach rightly draws attention to the fact that in circumstances where the connection of subsequent generators is not guaranteed but is required to make a SENE efficient it is likely to be preferable for generators to connect independent of a SENE to negate stranded asset risk.

What appears unclear, in the draft determination and the draft rule, is who has final control over the dimensions and design features of the SENE. The draft determination does not clarify who decides the final design of a SENE. The NGF would be supportive of the final design criteria being defined by the entity funding the SENE as opposed to the TNSP responsible for building the SENE.

Ownership, operation and control of a SENE

The NGF is not convinced that the revenue recovery and ownership arrangements will incentivise construction of SENE. Notwithstanding our view that SENEs are likely to be most viable in circumstances where there is a strongly demonstrated interest by multiple parties, on a smaller scale some degree of over-building may be a desirable investment risk for generators when connecting to the network. For instance, a single extension and connection may be built in a way that readily enables a second connection in that same location in the future.

However, given the lack of control over any over-build or SENE assets by a connecting generator, and the need to register as a TNSP, the incentive to pursue merchant transmission investment has again been lost. And as previously indicated by the NGF in the absence of such incentives we are not convinced that generators are likely to have a strong incentive to overbuild or to fund SENEs.

This issue does not appear to have been addressed by the AEMC.

We again reiterate our view that to improve the scope for merchant transmission investment, investors need both investment certainty and recognition of property rights. We believe this is a logical outcome, which can be facilitated within the NEM, and does not conflict with the open access regime.

Where an individual investor chooses to build a SENE type asset, that investor (or generator) should be provided with the entirety of the capacity right over that asset and be permitted to offer connection to other generators through private agreement or sale.

One of the major failings, in our view, of the transmission system is the inability of generators or investors to make private investments in transmission assets with any certainty that the value of that investment will not be captured by other beneficiaries or directly by new connections. As it relates to SENEs, we recommend that any party constructing a SENE type asset has its private property rights recognised in the form of full ownership of all available capacity rights.

In these circumstances, a generator wishing to connect at that location can choose to either duplicate an asset, which may be efficient depending on timing and cost, or make a private agreement with the owner of the privately-funded asset; whether that owner is a TNSP, a generator or another party.

Where spare capacity exists and will not be used in the future it will invariably be in the interests of the private owner of that asset to sell spare capacity. The sale price will always be capped by the price of building a duplicated asset. Thereby, it will actually reflect the absolute costs of transmission in that location (excluding shared network cost) which is an efficient signal.

The AEMC has failed to outline why such an approach is not appropriate even though the AEMC states 'that commercial arrangements with minimal regulatory intervention are desirable in competitive markets' (pg 25).

Negotiating connection to a SENE

The NGF notes the lack of clarity around the process for connecting to a SENE is indicative of the wider problems associated with the connections methodology and arrangements in the Rules. We note this issue requires clarification and resolution during the Transmission Frameworks Review.

Simplicity of the proposed approach

Leaving aside the issues that the NGF believes require further consideration, we agree that the preferred rule change, which reflects minimal change, is desirable as there is insufficient evidence to justify the original prosed rule change. Furthermore, that complexity was borne out in the extended debate on the many additional regulatory measures and additional prescriptions suggested by various parties. The avoidance of a burdensome regulatory outcome is welcomed.

Issue of transparency of costs and monopoly power

While the NGF supports the preferred approach as it avoids a new burdensome set of rules, we note that given it is wholly reliant on the current arrangements for negotiation and provision of services between TNSPs and market participants it will suffer from the existing limitations of those arrangements and problems associated with dealing with a monopolist.

While it is beyond the scope of this submission to detail those issues, we do hold some reservations that the negotiation between a SENE funder and a TNSP may be an impediment to actual funding progressing.

While we favour market approaches, including in this instance, unless a SENE funder can be assured the SENE design, size, precise location, and future revenue for the SENE funder are appropriate the SENE will not go ahead. While we appreciate that funding requirements incentivise TNSPs to meet the SENE funder's requirements it is unclear how this will play out in practice given NGF member experiences when negotiating stand-alone connections.

Case for not progressing the preferred rule

The NGF's support is based on the avoidance of a new burdensome regulatory outcome. In that regard, a view could be formed that investors and TNSPs may be able to progress SENEs in the absence of the preferred rule change by using the existing connections framework. In that sense improving the general connections framework in terms of information provision and determination of connection design would negate the need for this preferred rule change. If this was thought to be the case then the no rule would be necessary.

Conclusions

The NGF supports the draft determination subject to the issues raise in this submission.

The NGF is pleased to continue to provide advice to the AEMC in the consideration of these issues. Please do not hesitate to contact Mr Jamie Lowe, telephone (03) 9612 2236, or myself, telephone (02) 6232 7789, if you have queries in relation to this submission.

Yours sincerely,

M. Roberts

Malcolm Roberts
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