Vestas Australian Wind Technology Pty Ltd

13 May 2011

John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

By email: aemc@aemc.gov.au

Dear Mr Pierce

Submission: Strategic Priorities for Energy Market Development ["EMO0011"]

Vestas welcomes the opportunity to make a submission in response to the AEMC's Discussion Paper on Strategic Directions for Energy Market Development.

Vestas is the world's leading supplier of wind power solutions, having installed more than 40,000 wind turbines across the globe in more than 60 countries.

In Australia we have been responsible for the supply of more than half of the wind energy capacity to date, and we are currently working on Australia's largest wind farms including the 206 megawatt (**MW**) Collgar project and the 420 MW Macarthur project.

Vestas has made a number of submissions to recent AEMC consultations including the *Review of Energy Market Frameworks in light of Climate Change Policies*, the *Transmission Frameworks Review*, and the Scale Efficient Network Extensions (**SENE**) Rule change process.

In all of these consultations, many common themes have arisen, so many of our comments in response to this particular Discussion Paper may seem familiar to the reader.

The AEMC's three strategic priorities

Vestas does not disagree with the selection of any of the three strategic priorities nominated by the AEMC in the Discussion Paper. All are important in their own way, particularly the first (a predictable regulatory and market environment for rewarding economically efficient investment) and the third (ensuring the transmission framework delivers efficient and timely investment).

However, we consider that the AEMC would be well-advised to add two more strategic priorities to its list.

In particular, **reducing barriers to new entrants** should be a key focus of the AEMC from this point onwards. Adding this extra strategic priority would be an important admission that while the National Electricity Market began in December 1998, most of the market participants hold assets that were developed under quite a different set of rules, priorities and economic conditions.

Making the National Electricity Market (**NEM**) a more attractive place to invest for new entrants will also bring competition benefits for end users, and act to reduce the pace of the inevitable energy price rises forecast by the AEMC in the Discussion Paper.

Most of the transmission and distribution network assets in the NEM were funded and built by state governments, and many of the generation assets have a similar history. The present owners of these assets never had to seek planning permits, project finance, negotiate connection or power purchase agreements to get those investments off the ground. And they still don't pay use of system charges.

New entrants to the NEM face all of these hurdles, and new ones as well. For example, our customers (developers of new generation assets) tell us they find it very difficult to explain to financiers that the risk that future generation plant might connect nearby, resulting in generation constraints and/or significant deterioration to one's Marginal Loss Factor (**MLF**), are not material.

For new investors in renewable energy in particular, they are faced with more remote locations, and hence weaker grids and poorer loss factors. All of these contribute to economic barriers to new investment. Our customers tell us that MLFs are in fact becoming quite variable and unpredictable.

Another strategic priority for the AEMC should be **a less greenhouse gas intensive energy sector**. Reducing the level of greenhouse gases from the energy sector is a stated policy of all major political parties, yet this does not seem to have filtered down to agencies such as the AEMC just yet.

There is a very good reason why this has not yet occurred; the legislation governing the activities of the AEMC and other NEM agencies does not feature any explicit statement on greenhouse gases.

Accordingly, the AEMC appears unable to list this as a strategic priority at this stage. Rather, policies that seek to reduce greenhouse gases from the energy sector are a relevant factor for the AEMC but cannot presently be included as a strategic priority.

Policy background

It is important to point out that the AEMC's ability to properly respond to trends and shifts in the NEM and other energy markets that come within its jurisdiction is restricted by the legislation within which it operates.

In particular, the AEMC is required to have regard to the National Electricity Objective (**NEO**), set out in section 7 of the National Electricity Law (**NEL**):

> *The objective of this Law is to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to-*
>
> *(a) price, quality, safety, reliability and security of supply of electricity; and*
>
> *(b) the reliability, safety and security of the national electricity system."*

The NEO does not contain any references to the Australian Government's 20% Renewable Energy Target (**20% RET**), greenhouse emissions from the electricity sector, or any other kind of environmental matter. The focus of the NEO is firmly on the long term interests of electricity consumers, but only in the context of price, quality, safety, reliability and security of supply.

This in turn effectively excludes the AEMC from considering, for example, what kind of rule changes or other NEM reforms would be required in order to facilitate the achievement of the 20% RET by the year 2020. The difficult process involved in progressing the SENE Rule change is a good example of this dilemma.

As the Issues Paper for the AEMC's *Transmission Frameworks Review* stated:

> *The AEMC is required to have regard to the National Electricity Objective (NEO) in every review it undertakes and every change to the National Electricity Rules (NER or Rules) that it assesses.* ***The NEO will therefore form the overarching principle*** *for the assessment framework used to evaluate potential transmission reforms.*

As the Australian Energy Market Operator (**AEMO**) explains in its *Introduction to Australia's National Electricity Market*, NEM institutions like the AEMO and AEMC are prevented by the NEO from giving effect to policies or legislation such as the 20% RET that favour one kind of fuel source (renewable energy) over others:

> *AEMO's charter focuses specifically on efficiency, security and reliability of power supply, and excludes favouring one fuel source over any other. Consequently, AEMO has neither the power nor the authority to make decisions based on considerations of sustainability and balance in resource management.*

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So, while the AEMC and the AEMO are both able to take note of policies and legislation such as the 20% RET as a notable development and "the driving force behind new investment in renewable generation" (the wording used in the 2010 AEMC consultation paper on the SENE Rule change proposal), those agencies cannot propose or implement any reforms to reduce greenhouse gas emissions or help successfully deliver policies such as the 20% RET if those reforms would work in any way against the NEO.

That fundamental conflict means that the AEMC is unlikely to be able to propose reforms that will ensure Australia lifts its proportion of electricity generation from renewable sources from the current level of approximately 8% to the required 20% by the year 2020, as set out in the Australian Government's 20% RET policy and legislation.

The 20% RET legislation, passed with bipartisan support, stipulates an increase in (and hence, unashamedly gives primacy to) renewable energy generation. But the NEL (and in particular the NEO) takes a completely neutral stance.

Unless and until the NEL is amended to include some weight, relevance or value ascribed to the achievement of Government policies such as the 20% RET, then NEM agencies like the AEMC and the AEMO have got their hands tied.

Those agencies are bound to make their decisions and carry out their work in line with the NEO, not with the 20% RET. Where there is a conflict between government policy and the NEO, this also means they are duty bound to ignore government policies that is inconsistent in any way with the NEO – especially something like the 20% RET that mandates an increase in one kind of fuel source (renewable energy) over all others.

Agencies like the AEMC and the AEMO are well aware that the Government has policies in place to change the electricity generation mix and increase the level of renewable energy. Their publications in 2009 and 2010 make this clear.

But the NEO in its current form compels these agencies to ignore policies like the 20% RET in their decision-making processes.

This is not the fault of the AEMC or of the AEMO, nor is it something those agencies are able to address.

If the Australian Government and other members of the Ministerial Council on Energy (**MCE**) want the target of 20% renewable energy to be met by the year 2020, they cannot expect agencies like the AEMC, AEMO and the AER to play any significant part in this effort if it would require any steps to be taken that the NEO would not otherwise compel.

Instead, Vestas considers that the MCE should amend the NEL and other relevant energy legislation to include an amended NEO, one that perhaps addresses matters such as greenhouse emissions from the energy sector and the promotion of renewable energy.

Next steps

Vestas staff would be pleased to meet with AEMC staff to discuss our submission and answer any other questions they may have. Please contact the writer on (03) 8698 7300 to do so.

Yours sincerely,

[signed]

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