Reserve Capacity Mechanism Working Group

Minutes

Meeting No.	10
Location:	IMO Boardroom Level 17, 197 St Georges Terrace, Perth
Date:	Thursday 28 February 2013
Time:	Commencing at 2.05pm – 3.50pm

Attendees	Class	Comment
Allan Dawson	Chair	
Kate Ryan	IMO (replacing Suzanne Frame)	
Brad Huppatz	Market Generator (Verve Energy)	
Ben Tan	Market Generator	
Andrew Sutherland	Market Generator	
Shane Cremin	Market Generator	
Wendy Ng	Market Customer	
Steve Gould	Market Customer	
Stephen MacLean	Market Customer (Synergy)	
Andrew Stevens	Market Customer/Generator	
Geoff Gaston	Market Customer	Proxy
Jeff Renaud	Demand Side Management	
Geoff Down	Contestable Customer	
Brendan Clarke	System Management	
Wana Yang	Observer (Economic Regulation Authority)	
Paul Hynch	Observer (Public Utilities Office)	
Apologies	**Class**	**Comment**
Justin Payne	Contestable Customer	
Also in attendance	**From**	**Comment**
Fiona Edmonds	Observer (Alinta)	
Mike Thomas	Presenter (The Lantau Group)	
Aditi Varma	Minutes	
Greg Ruthven	Observer (IMO)	
Natasha Cunningham	Observer (IMO)	
Johan van Niekerk	Observer (IMO)	
Neetika Kapani	Observer (IMO)	
Oscar Cleaver-Wilkinson	Observer (IMO)	

Item	Subject	Action
1.	**WELCOME AND APOLOGIES / ATTENDANCE** The Chair opened the tenth and final meeting of the Reserve Capacity Mechanism (RCM) Working Group (RCMWG) at 2.05pm. The Chair welcomed the members in attendance and noted an apology from Mr Justin Payne. The Chair introduced the newly appointed Group Manager of Development and Capacity, Ms Kate Ryan to the meeting and acknowledged observers present from the IMO's System Capacity team and Alinta.	
2.	**MINUTES ARISING FROM MEETING 9** The minutes were accepted as a true record of the meeting. Mr Brad Huppatz observed it was difficult to remember the discussions at the meeting as the minutes were circulated three months after the previous meeting. The Chair apologised on behalf of the IMO and responded that the organisational restructure at the IMO in December 2012 had an impact on some work processes. He further noted that the minutes from this meeting would be circulated much sooner. *Action Point: The IMO to publish minutes of RCMWG meeting no.9 on the Market Web Site.*	**IMO**
3.	**ACTIONS AND DECISION REGISTER** Ms Wendy Ng noted that Alinta had requested for an extension on the timeframe for members to respond to the email circulated by the IMO on 7 December 2012. Ms Ng noted that while she had received a response from the IMO she understood from the response that Alinta were not to be provided with an extension. Ms Ng would like her name to be removed from the summary of responses on page 16 and added to the list of non-responders on page 17. The Chair responded that this meeting was a result of requests received from Alinta and other members. The Chair added that the IMO Board was notified in December 2012 on progress made, however, it was highlighted that a further RCMWG meeting had been scheduled to resolve the outstanding issues. This meeting had been organised in response to requests to deal with outstanding issues The Chair noted that the IMO would progress key proposals to the Rule Change process. He added that objections raised by members had been minuted; however, there would be further opportunities to raise issues during consultation periods in the Rule Change Process.	
4.	**AGENDA ITEM 5 : Reserve Capacity Price and Dynamic Refund Mechanism** The Chair invited Mr Mike Thomas to introduce his memorandum, which had been distributed with the meeting papers. The following discussion points were noted: • Mr Andrew Sutherland queried why there were negative percentage values on the x axis of representing excess capacity when the IMO must procure capacity up to the Reserve Capacity Requirement under the Market Rules. Mr Greg Ruthven responded that the IMO would only run a Reserve Capacity Auction if capacity had been offered into the auction in the Bilateral Trade Declaration process. Mr Ruthven noted, however,	

	that the Reserve Capacity Price would be 85% of the Maximum Reserve Capacity Price (MRCP) under the current mechanism if there was a shortfall of capacity and no auction was held. In response, Mr Sutherland noted that it seemed unlikely that anyone would offer capacity into the auction. It was further discussed that the Supplementary Reserve Capacity process would be held to procure enough capacity to meet the Reserve Capacity Requirement. • Mr Sutherland also queried if the uplift for the proposed Reserve Capacity Price (RCP) regime of 110% would be a strong enough incentive for encouraging bilateral contracts in the market. Mr Geoff Gaston noted that the curve did not provide an adequate incentive for bilateral contracting from both a retailer's and a generator's perspective. Discussion ensued on the nature of bilateral contracting that could be expected in excess and shortfall capacity situations and whether the curve should start at a higher point than 110%. Mr Thomas noted that the issue seemed to be centralised on the premise that by not contracting, there would be less investment and thus there would be a reduction in the reserve margin. Mr Gaston responded that the graph did not appear to be solving the excess capacity issue. He did not believe that a reduction in the price would simultaneously reduce excess capacity. He further added that the MRCP had reduced over the past couple of years and this model added to that volatility in the market. The Chair noted that the MRCP reduction was due to the erroneously calculated transmission cost component that had caused temporary inflations in the price. He further noted that the MRCP calculation methodology was not reviewed to manage excess capacity. • Mr Ben Tan echoed Mr Sutherland's point and added that he did not believe that the axis was robust enough on the upside to encourage retailers to contract bilaterally. Mr Shane Cremin noted that the increase from an 85% adjustment factor to a 110% adjustment factor was a substantive change in the right direction. But he also agreed with Mr Sutherland on the point that the incentive to contract bilaterally might be too weak thereby increasing merchant risk and no new generating plants being built. Mr Stephen MacLean considered that the discussion point was moot because what generators should aim for is a firm capacity price over a long period. Mr Andrew Stevens noted that there would never be a time when there would be equal incentive for a retailer and a generator to contract bilaterally. • Mr Gaston and Mr Tan registered their concern regarding increasing merchant risk. Mr Cremin noted that the increase in risk would then lead to shortage in capacity which would then encourage the retailer to start contracting because the retailer would tend to avoid a Supplementary Reserve Capacity auction scenario. He added that government policy decisions also play a role in the market. Mr Tan and Mr MacLean agreed with Mr Cremin's point. Ms Wendy Ng observed that many customers are opting for a direct pass-through of capacity charges, which also influences the retailer's willingness to contract bilaterally. • Mr Sutherland noted that the proposal was better than the current regime; however the electricity industry required long term financing arrangement and thus required bilateral contracts to ensure certainty for revenue. • On the dynamic refunds regime, Mr Stevens stated that he did not	

	support the minimum refund factor of 1 but would support a value that could be affected by either an availability factor or capacity factor determined in relation to a recent time period, the intrinsic value of the assets and their availability or performance. A generating plant that was late to arrive into the market would have an availability or capacity factor of zero and would effectively get charged one times the multiple of its factor. Mr Sutherland added that a minimum refund factor of 1 would only be fair if the maximum was modified every year. Mr Brad Huppatz also did not agree with 1 being the minimum refund factor because any number above zero itself is an incentive to make generation available. Discussion ensued on the validity and application of the minimum refund factor value being 1. Mr Cremin observed that the philosophy behind The Lantau Group's proposal is based on the fact that different value needs to be assigned to different generating plants based on their reliability in providing capacity when needed. • Mr Gaston agreed with the idea of dynamic refunds but questioned the recycling component of the model. He observed that there would be much greater risk of a plant tripping while running. • Mr Thomas noted that reducing the minimum refund factor to zero will make the nature of forced outages even more random without giving an incentive to make plant available. Mr Huppatz and Mr Gaston noted that the overall magnitude of the refunds matter, not the scale. Mr Stevens agreed and noted that the minimum refund factor would only come into play when the reserve margin is so large that the economic value of the capacity is low. Mr Cremin noted that the level of capacity refunds is itself the incentive to correct a random event, not the randomness itself. Mr Sutherland argued that extending the logic of forced outages being random; the refund factor should just be 1 and not different at different times. He queried the logic behind keeping the maximum at 6, to which Mr Thomas responded that the maximum factor of 6 was already built in the rules. The Chair noted that members should keep in mind that the refund revenue was also getting recycled. The Chair offered that the IMO will revisit the proposed minimum refund factor prior to submitting any rule changes. • Mr Gaston questioned how the recycling of refunds would tie in with the Shared Reserve Capacity Cost. Mr Thomas responded that the proposed package should improve the generation offer stack and improve efficiency. He further added that if the package works well, then retailers would benefit, however if the package does not work well then everybody would be worse off. Over time, if excess capacity was being supplied into the market, the Reserve Capacity Price would come down. • The Chair asked members to put forward any further comments on the overall package. Mr Gaston noted his objection to harmonisation and sought clarification pertaining to the scenarios in which Demand Side Management (DSM) would be called on. The Chair responded that System Management would have discretion over which Facilities it would dispatch and what fuel sources it would preserve in a High Risk or Emergency Operating State. • Mr Tan noted that he was happy with the proposed package, however was concerned with the uplift of 110% and believed that	

	a higher number needed to be incorporated into the model. Ms Wendy Ng questioned if a floor was considered to be included in the model. The Chair responded that it had been discussed in previous meetings but the final proposal did not include a floor price. • Dr Steve Gould sought clarification on what constituted as eligible available capacity. The Chair clarified that this was all capacity that was made available in the Balancing Merit Order, and would exclude DSM and Intermittent Generation (i.e., capacity that has a Reserve Capacity Obligation Quantity- RCOQ of zero). • Members sought clarification on how the transitional arrangements would work. The Chair clarified that this proposal would appear to qualify for the transitional arrangement policy. He added that the dynamic refunds regime would commence but the recycling of refunds would be transitioned over a three year period. • Mr Stevens questioned if there had been any confirmation on the conditions when DSM would be dispatched. He asked for more clarity on what would be the level of reserve margin in a Trading Interval for System Management to consider dispatching DSM. The Chair responded that the IMO would revert to the RCMWG with more detail during the Pre Rule Change Process. • The Chair added that the next step forward would be to present the package to both the IMO Board and the Market Advisory Committee (MAC). He added that the next step will incorporate the development of Pre Rule Change Proposals to take forward to the formal submission process. *Action points:* • *The IMO to present the summary of recommendations to the IMO Board and the MAC.* • *The IMO to revisit the proposed minimum refund factor prior to submitting any rule changes.* • *The IMO to revert to the RCMWG with more detail during the Pre Rule Change Process.*	 **IMO** **IMO** **IMO**
	CLOSED The Chair thanked the members and declared the meeting closed at 3.50 pm.	