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Oates Review:
Market rules discussion paper

Presentation to MAC 20 January 2010

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Role of the discussion paper

- **Primarily a “think piece”**
- **Documents understanding of issues**
- **Documents design perspective**
- **Highlights preliminary views on:**
  - “Pinch points” in current design
  - Characteristics (but not specifics) of solutions

Holistic regulatory/design view

- **The sector design is formed from the net impact of :**
  - Legislation
  - Licences
  - Policy (e.g. Renewables, capacity caps)
  - Regulations
  - Market rules
  - Structure
    - Ownership, technology mix, fuel supply
  - Regulatory and operational expertise/training/governance approach
    - E.g. Laissez faire v heavy handed
  - Transition arrangements including vesting and displacement

All parts play a role – market rules are "glue" between many of the parts

Framework

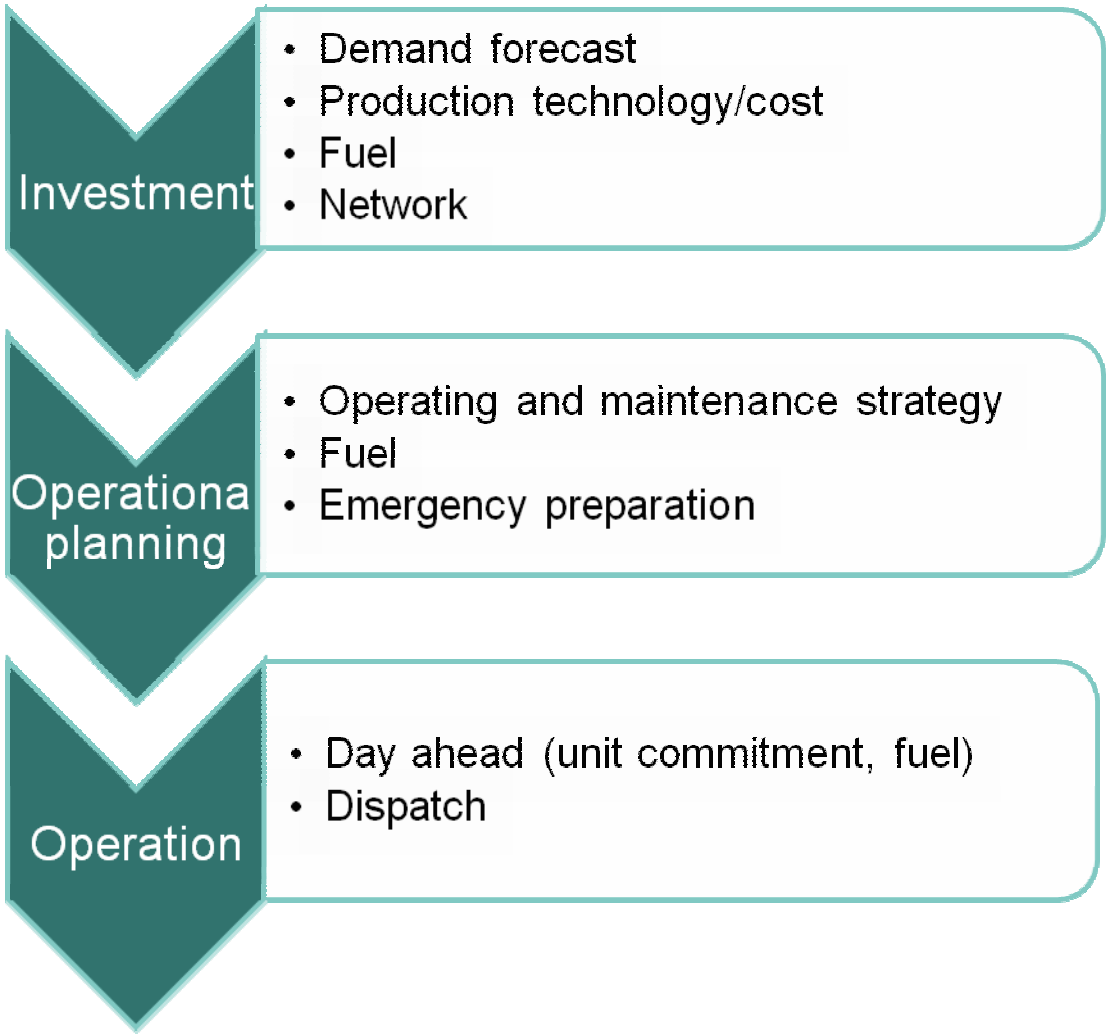
- **Framework based on analysis of fundamentals of the industry and impact of operation on reliability and efficiency**
- **Market is a tool to deliver**
- **Market implies commercial incentives used to influence behaviour**
- **Commercial incentives = profit motive**

Starting points

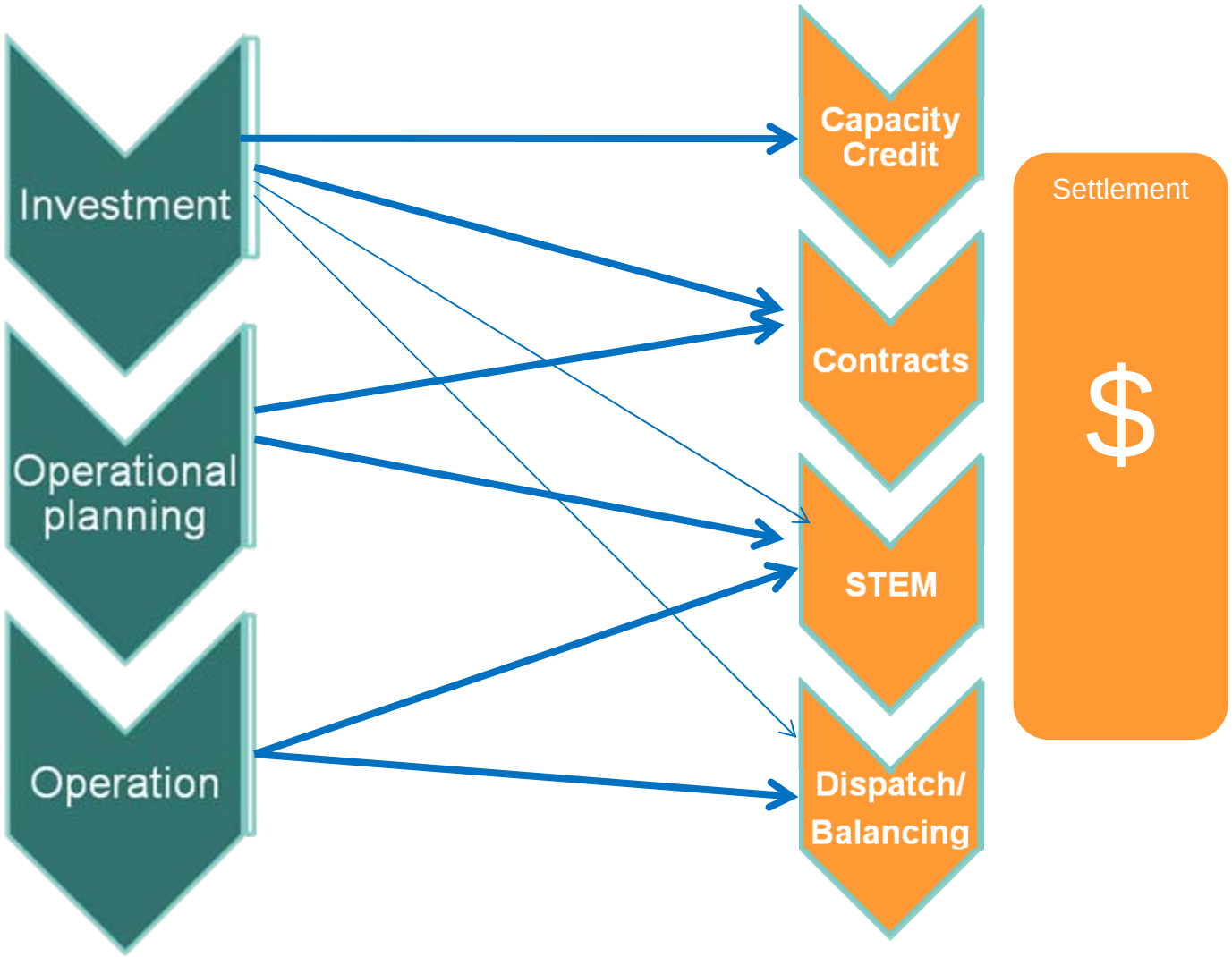
- **Identified unacceptable outcomes in current arrangements**
  - Verve Review conclusions
  - IMO market evolution plan
  - Multi-faceted problem (vesting/displacement, sector strategy, market rules)
  - Ministerial mandate to address
- **(for the record) Core market design not under review**
  - No mandate
  - Avoid throwing “baby out with bathwater”
  - Repair/evolve implementation of core design
    - Rules for many market designs are repaired/evolved in first few years
- **Existing governance process respected**
  - Market rules MUST comply with market objective

    No bias for or against different participant(s) !

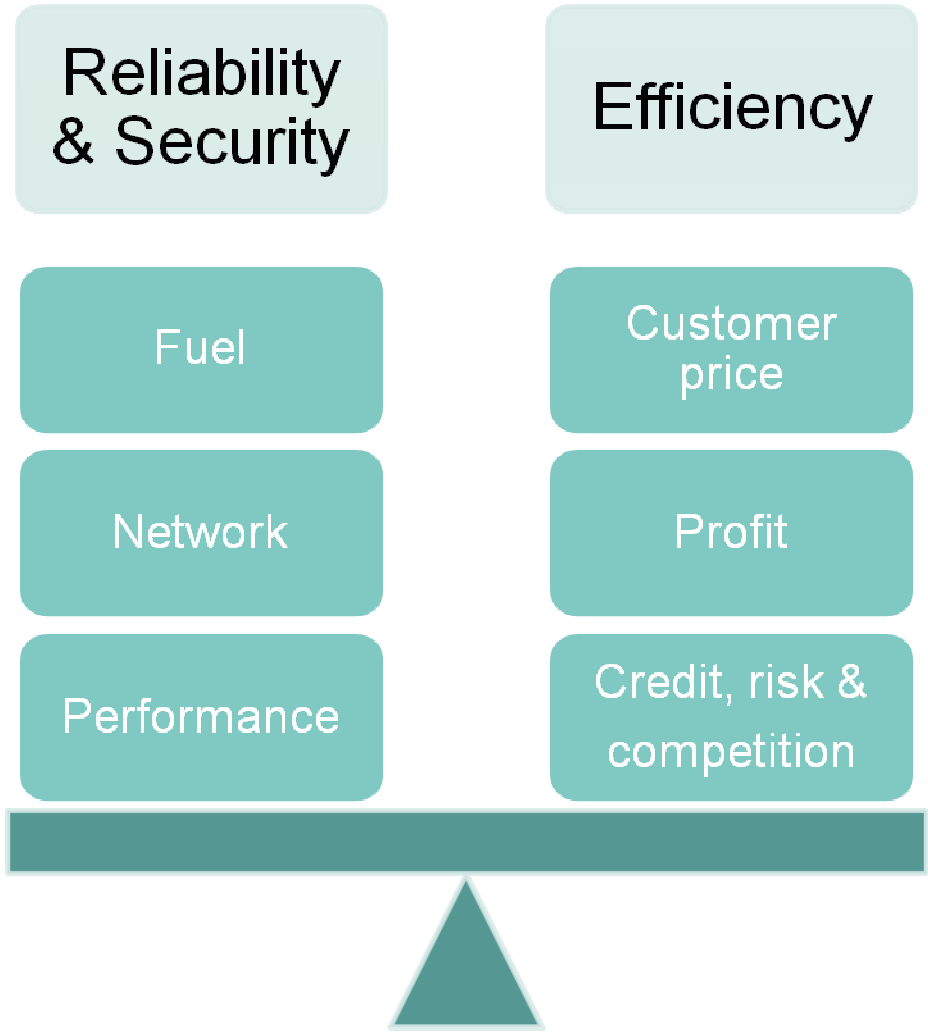
Industry steps



Using the WEM to deliver industry steps

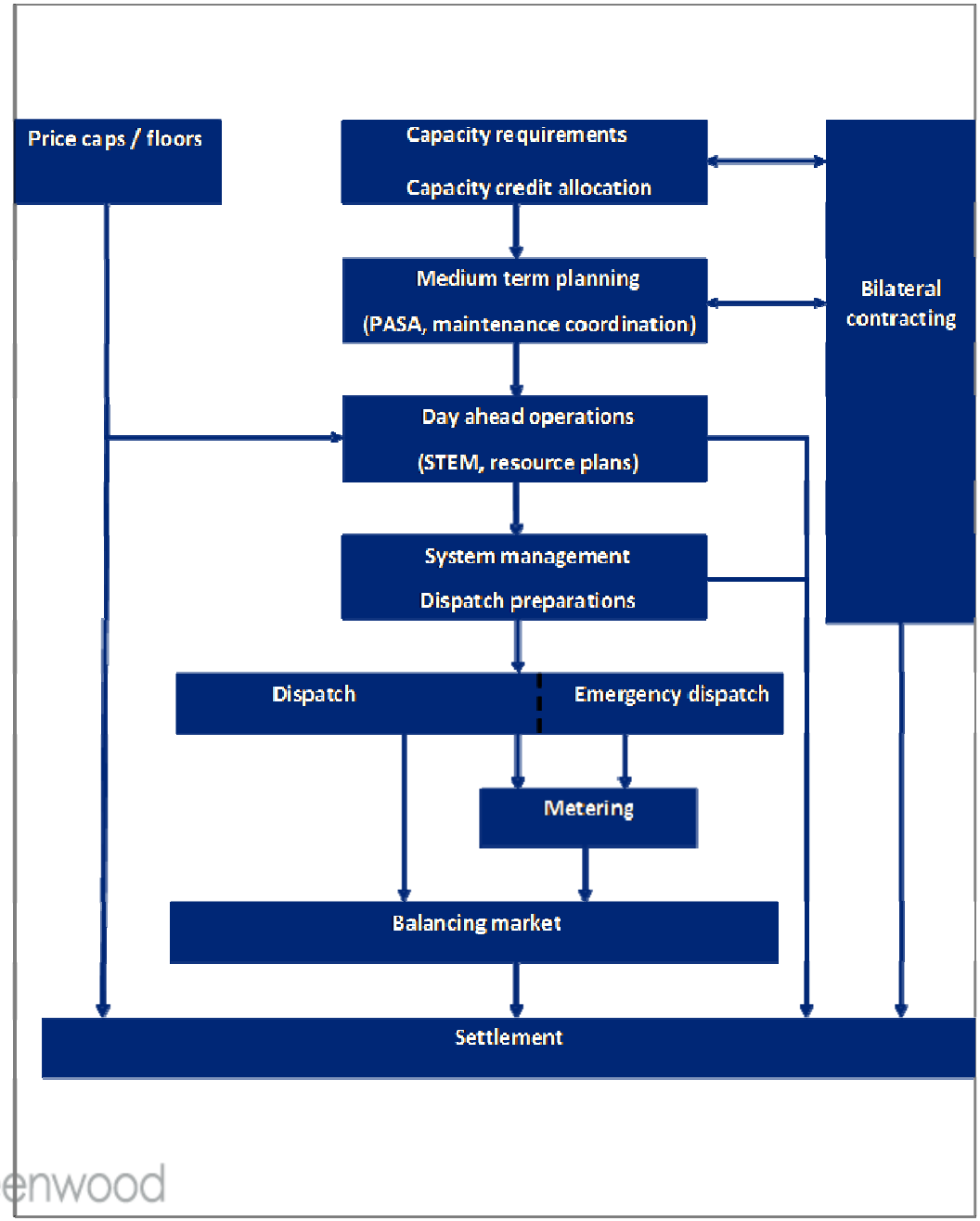


A difficult balance



WEM design elements and linkages

(ref discussion paper)



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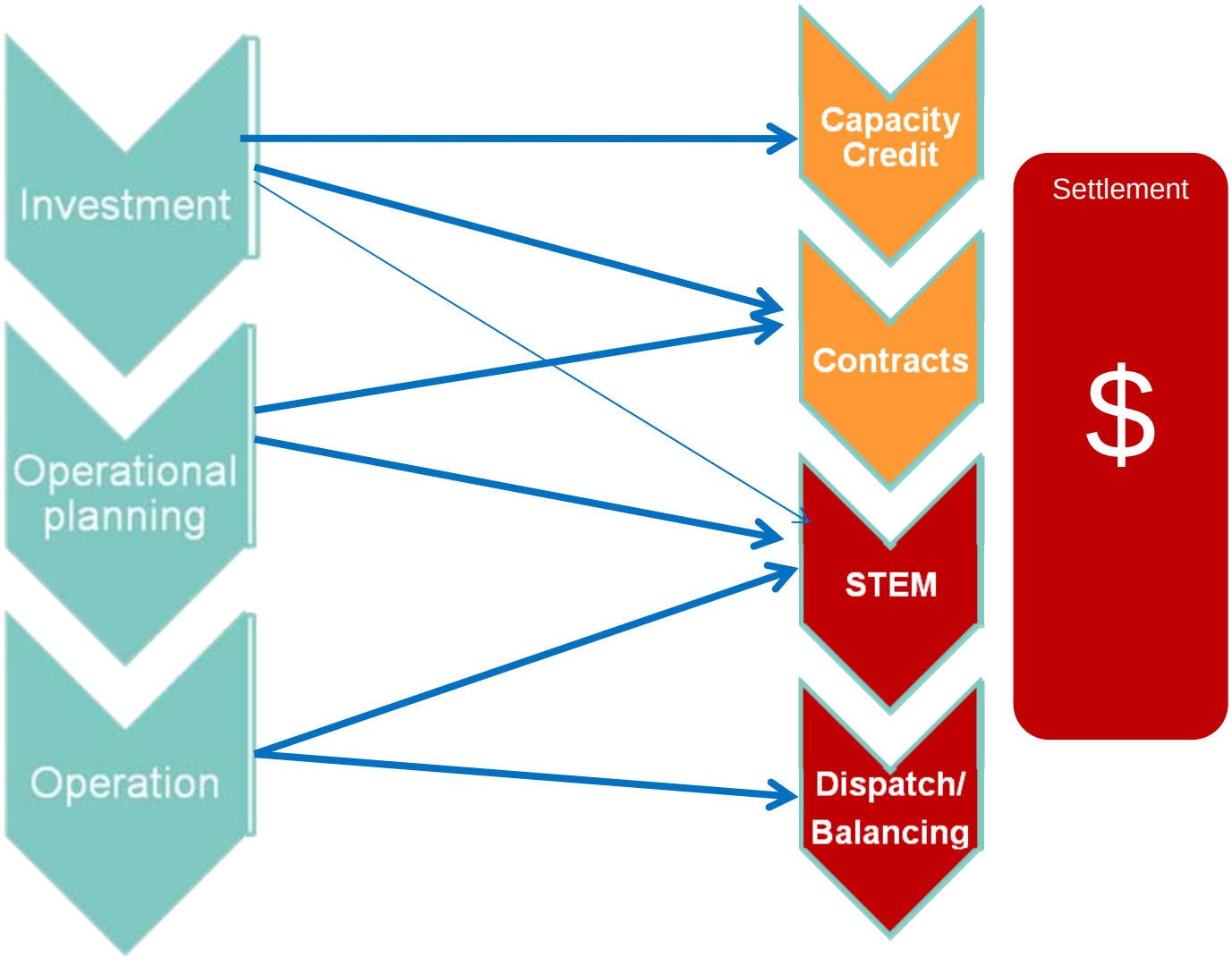
Focus on short term operations

Using the WEM to deliver industry steps



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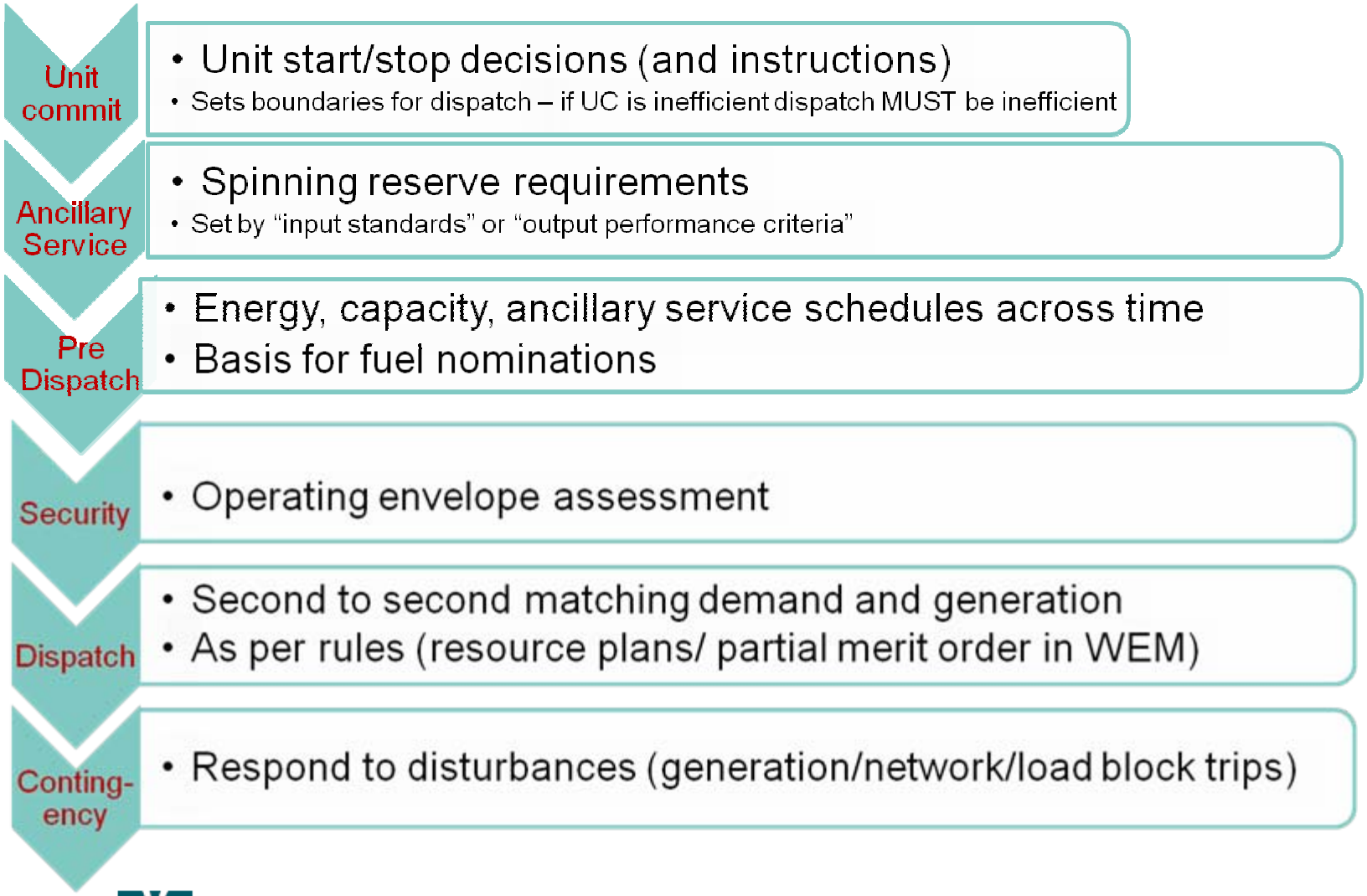
Short term operations



WEM cost and revenues (short term operations)

- **Operating expenditure (including for fuel);**
- **Ancillary Service related expenditure (capital and operating);**
- **Capacity credit revenue;**
- **Capacity credit penalties;**
- **Net revenue from off market bilateral contract trading;**
- **Bilateral contract payments;**
- **STEM trades;**
- **Net DDAP/ UDAP revenue in balancing;**
- **Ancillary service revenue; and**
- **Network charges and market fees; and**
- **Ancillary Service charges**

Illustrative strawman issues for discussion

not intended to be comprehensive at this stage

	Status Quo	Issue	Sample options Subject to CBA
Unit Commitment	IPP: Embedded in resource plans based on single pass or SM override on tech grounds. Verve: Opaque, not optimised with IPP.	Little chance for economic optimisation	STEM gate closure (time and no.) Security constrained STEM
Ancillary Service		Little chance for economic optimisation	
Pre dispatch	Single pass . Basis for security assessment but information only for market	Too late for some fuel management	
Security Assessment	By SM after market gate closure hence no commercial mechanism for market to fix – presumes very few issues ?	Heavy reliance on intervention to address	Incorporate in STEM
Dispatch & Balancing	Based on resource plan Verve as primary balancer	Misses economic options for IPP participation	Broaden option for participation. Balancing support contracts. Economic dispatch
Settlement	Static capacity penalties and all “stick no carrot” UDAP, DDAP factors, allocation of Anc S charges not cost reflective	Commercial rewards and penalties inefficient (materiality?) hence market missing efficient behaviours	Adjust magnitude of payments

WEM Unit Commitment

- **Non Verve: embedded in STEM submissions and resource plans**
  - Heavily influenced by (bilateral) contract positions
- **Verve: effectively determined by System Management to meet dispatch/security/balancing requirements**
- **System Management required to consider physical operating conditions**
- **Non Verve IPPs have no price discovery**
  - Essential for efficient unit commitment
    - Central UC
    - Multiple passes
    - Liquid trading

Reiterate

- **Holistic design essential**
  - Market rules
  - Contract base
  - Vesting (part of transition)
  - Regulation
    - Retail price (including cost reflectivity)
    - Contestability policy
    - Network augmentation
    - Network pricing (quantum and design)
- **Many aspects of market working in principle**
- **Existing governance structure respected**
  - Practical
  - Important for credibility of industry

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Now, the hard work !!