

Independent Market Operator



Rule Change Notice

Title: Maximum Reserve Capacity Price Methodology and Review

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1. INTRODUCTION

Market Rule 2.5.1 of the Wholesale Electricity Market Rules provides that any person (including the Independent Market Operator) may make a Rule Change Proposal by completing a Rule Change Proposal Form and submit this to the Independent Market Operator (IMO).

The IMO will assess the proposal and, within 5 Business Days of receiving the Rule Change Proposal Form, will notify the proponent whether the Rule Change Proposal will be progressed further.

In order for the proposal to be progressed the change proposal must explain how it will enable the Market Rules to better contribute to the achievement of the Wholesale Market Objectives. The objectives of the market are:

- (a) to promote the economically efficient, safe and reliable production and supply of electricity and electricity related services in the South West interconnected system;
- (b) to encourage competition among generators and retailers in the South West interconnected system, including by facilitating efficient entry of new competitors;
- (c) to avoid discrimination in that market against particular energy options and technologies, including sustainable energy options and technologies such as those that make use of renewable resources or that reduce overall greenhouse gas emissions;
- (d) to minimise the long-term cost of electricity supplied to customers from the South West interconnected system; and
- (e) to encourage the taking of measures to manage the amount of electricity used and when it is used.

A Rule Change Proposal can be processed using a Standard Process or a Fast Track Process. The Standard Process involves a combined 10 weeks public submission period, while the Fast Track Process involves the IMO consulting with Rule Participants who either advise the IMO that they wish to be consulted or the IMO considers have an interest in the change.

2. THE RULE CHANGE PROPOSAL

2.1 *The Submission*

The IMO submitted, on 15 October 2007, a Rule Change Proposal to allow the results of a review conducted to assess the appropriateness of the parameters used to determine the Maximum Reserve Capacity Price to be considered when revising the Maximum Reserve Capacity Price.

This Rule Change Notice is published according to Market Rule 2.5.7, which requires the IMO to publish a notice within 7 Business Days of receiving a Rule Change Proposal.

2.1.1 *Submission details*

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Date Submitted:	15/10/2007
Urgency:	High

2.2 *Details of the Proposal*

Clauses 4.16.3 and 4.16.4 of the Wholesale Electricity Market Rules provide for an annual review to be conducted by the IMO to assess the appropriateness of some of the parameters that are used to determine the Maximum Reserve Capacity Price. The next clause, 4.16.5, provides a mechanism by which the IMO proposes a revised Maximum Reserve Capacity Price. However, the linkage between the review and the proposal of the revised value could be enhanced.

The IMO has also established an industry-based Advisory Group to assist in a more general review of the Maximum Reserve Capacity Price. One of the outcomes of this review has shown that the methodology used to estimate the capital cost of an Open Cycle Gas Turbine (OCGT) power station currently under-estimates the real cost of building such a plant. This has resulted from a change in the construction and engineering environment over the past few years. In this case, applying the methodology outlined in Appendix 4 of the Wholesale Electricity Market Rules would result in an outcome that is not reflective of today's construction and engineering cost environment.

Therefore, this rule change proposal aims to introduce a mechanism by which the outcome of the review can be considered when revising the Maximum Reserve Capacity Price and to take account of methodology changes if they are significant and can be substantiated.

A significant change to the methodology would be one where the IMO provides evidence that the application of the existing methodology would have a material impact on the Maximum Reserve Capacity Price, and where adjusting the methodology better supports the Wholesale Electricity Market Objectives. Changes

to the methodology will be limited to the parameters that are reviewed each year under clause 4.16.4 of the Wholesale Electricity Market Rules.

The review conducted in accordance with clause 4.16.3 and 4.16.4 of the Wholesale Electricity Market Rules for the 2008 Reserve Capacity Cycle (for capacity that will be available from 1 October 2010 to 1 October 2011) has already commenced. The IMO's draft report, to be published in early November, will propose a revised value which will be subject to public consultation (in accordance with clause 4.16.6).

Submissions made by interested parties will then be taken into consideration when the IMO produces its Final Report and final revised Maximum Reserve Capacity Price for approval by the Economic Regulation Authority.

The rule amendments proposed by the IMO are outlined in section 5 of this Notice.

2.3 The Proposal and the Market Objectives

In addition to improving the clarity of the Wholesale Electricity Market Rules and removing doubt about the application of the findings of the review of the Maximum Reserve Capacity Price, the IMO considers that the objectives of the market as set out in clause 1.2.1 of the Wholesale Electricity Market Rules will be addressed by this proposed rule change as follows:

- (a) *to promote the economically efficient, safe and reliable production and supply of electricity and electricity related services in the South West interconnected system.*

The Reserve Capacity Mechanism is an important component of the Wholesale Electricity Market and measures taken to ensure that the Maximum Reserve Capacity Price is cost-reflective will further the achievement of this objective.

- (b) *to encourage competition among generators and retailers in the South West interconnected system, including by facilitating efficient entry of new competitors.*

The IMO considers that this rule change proposal supports objective (b) of the Wholesale Electricity Market Rules by encouraging the efficient entry of new facilities (and new competitors) into the Wholesale Electricity Market.

- (c) *to avoid discrimination in that market against particular energy options and technologies, including sustainable energy options and technologies such as those that make use of renewable resources or that reduce overall greenhouse gas emissions.*

The IMO considers that the proposed changes do not impact on, and therefore are consistent with, the operation of objective (c) of the Market Objectives.

- (d) *to minimise the long-term cost of electricity supplied to customers from the South West interconnected system*

The IMO considers that through the expected positive contribution to the achievement of objectives (a) and (b), the proposed changes are consistent with the operation of objective (d) of the Market Objectives.

- (e) *to encourage the taking of measures to manage the amount of electricity used and when it is used.*

The IMO considers that the proposed changes do not impact on, and therefore are consistent with, the operation of objective (e) of the Market Objectives.

3. WHETHER THE PROPOSAL WILL BE PROGRESSED FURTHER

The IMO has decided to proceed with this proposal on the basis that the IMO's preliminary assessment indicated that the proposal is consistent with the Market Objectives.

The IMO has decided to process this Rule Change Proposal using the Fast Track Process, described in section 2.6 of the Wholesale Electricity Market Rules, on the basis that it satisfies the criteria in section 2.5.9(c) of the Rules.

Section 2.5.9 states:

The IMO may subject a Rule Change Proposal to the Fast Track Rule Change Process if, in its opinion, the Rule Change Proposal:

- (a) is of a minor or procedural nature; or*
- (b) is required to correct a manifest error; or*
- (c) is urgently required and is essential for the safe, effective and reliable operation of the market or the SWIS.*

In order to achieve an efficient outcome when setting the Reserve Capacity Price for the next capacity cycle, this rule change must be progressed before the IMO provides its Final Report on the Maximum Reserve Capacity Price to the Economic Regulation Authority for approval. The IMO considers that this change, therefore, is urgently required and essential in order to set effective and efficient Maximum Reserve Capacity Price for the 2010/11 Reserve Capacity Cycle.

As this change relates to a protected provision, see clause 2.8.13 in the Market Rules, any change resulting from this proposal must be approved by the Minister for Energy after the Final Report is published.

The projected timelines for processing this proposal are:

- This Rule Change Notice published 22/10/2007
- Consultation period 23/10/2007 - 12/11/2007
- Final Report published 19/11/2007
- Final Report approved by the Minister 17/12/2007

4. CONSULTATION

Any Rule Participant wishing to be consulted regarding this rule change is invited to notify the IMO within 5 Business Days of this notice being published.

The IMO prefers to receive notifications for consultation by email to **marketadmin@imowa.com.au**.

Notifications may also be sent to the IMO by fax or post, addressed to:

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Attn: Dora Guzeleva, Manager Market Administration
PO Box 7096
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Fax: (08) 9254 4399

5. PROPOSED AMENDING RULE

The IMO proposes the following change to the Wholesale Electricity Market Rules (~~deleted wording~~, added wording):

Clause 4.16.5

- 4.16.5 The IMO must propose a revised value for the Maximum Reserve Capacity Price using the methodology described in Appendix 4 after taking into account any significant modifications to the methodology resulting from the review conducted in accordance with clause 4.16.3 and 4.16.4.