INDEPENDENT MARKET OPERATOR

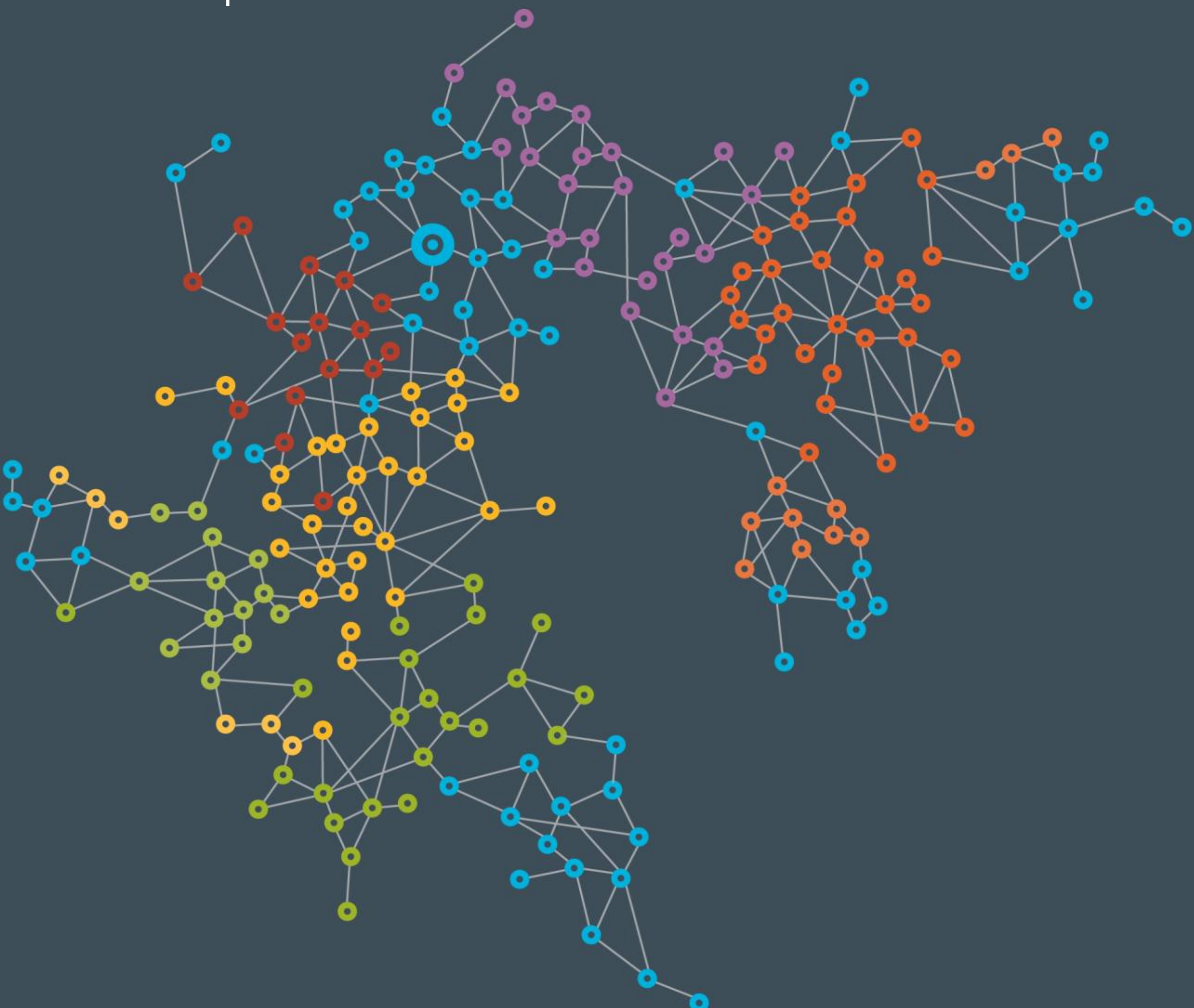
Final Rule Change Report

Title: Limits to early entry capacity payments

RC_2012_10

Standard Rule Change Process

Date: 3 September 2013



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The Reserve Capacity Mechanism requires credited capacity to be available from the first day of the Capacity Year (1 October). To encourage the timely arrival of new capacity, Facilities may enter the market and begin receiving capacity payments at any time during the four month period leading up to this date (1 June to 30 September).

Synergy proposed amendments to clause 4.1.26 of the Market Rules to limit early capacity payments between 1 June and 30 September to Scheduled Generators and Non-Scheduled Generators only. Under Synergy's proposal other capacity types, such as Demand Side Programmes (DSPs), would only be entitled to capacity payments from 1 October.

Consultation

The Pre Rule Change Proposal was discussed by the Market Advisory Committee (MAC) at its 13 June 2012 meeting. MAC members agreed that the proposal should be submitted into the formal rule change process.

The Rule Change Proposal was submitted on 14 June 2012 and the Rule Change Notice published on 22 June 2012. In the Rule Change Notice, the IMO also sought the views of interested parties on the concept of removing early capacity payments for all capacity types, including generation.

The first submission period was held between 25 June 2012 and 3 August 2012. Submissions were received from APA Group, Community Electricity, EnerNOC, Griffin Power, Perth Energy, Synergy and Verve Energy. APA Group, Community Electricity, Perth Energy, Synergy and Verve Energy supported the Rule Change Proposal while EnerNOC and Griffin Power opposed it.

None of the submitting parties expressed support for the complete removal of early capacity payments, apart from Synergy who considered it one of a number of options worthy of further consideration. There was however wider support for changes to remove early capacity payments during times of excess capacity, while retaining the option to make these payments available at other times.

At the 8 August 2012 MAC meeting, Synergy presented a concept paper exploring further options for improving the cost-benefit trade-off of early capacity payments. During the discussion the Public Utilities Office (PUO) noted that the issue seemed to be a fundamental market policy issue rather than an operational issue. The PUO offered to consider the issue of incentivising early entry of capacity and provide the MAC with details on the next steps in the process for addressing the issue from a policy perspective at the next meeting.

During the 12 September 2012 MAC meeting, the PUO advised MAC members that it would be most appropriate to await the outcomes of the Reserve Capacity Mechanism Working Group (RCMWG) before providing any policy direction. The IMO extended the timeframes for the preparation of the Draft Rule Change Report accordingly.

The final meeting of the RCMWG was held on 28 February 2013. On 8 May 2013, the PUO confirmed that the IMO should continue to progress the proposal and its counter-proposals. The IMO received no policy direction in relation to the issue.

The Draft Rule Change Report was published on 4 June 2013 and the second submission period was held between 5 June 2013 and 30 July 2013. Submissions were received from Alinta Energy, Synergy and Verve Energy, all supporting the proposal.

Assessment against Wholesale Market Objectives

The IMO considers that overall the proposed amendments are inconsistent with the Wholesale Market Objectives. While the removal of early capacity payments may reduce costs and so benefit Wholesale Market Objectives (a) and (d), in times where the market is in danger of not meeting its Reserve Capacity Target any potential savings may be outweighed by the associated risks to system reliability and the potential need to seek supplementary capacity.

On the other hand, in times of excess capacity the potential benefits of removing early capacity payments would appear to apply to all forms of capacity. The IMO is not convinced that under either scenario there is justification for allowing early capacity payments for generators only, and so considers that the proposal discriminates against demand side capacity and therefore has a strong negative impact on Wholesale Market Objective (c) which outweighs any potential benefits to other Wholesale Market Objectives.

Practicality and cost of implementation

The IMO has not identified any additional costs associated with the implementation of the Rule Change Proposal.

EnerNOC identified a significant negative financial impact, in excess of $1 million, if the amendments were implemented as proposed and affected Reserve Capacity Cycles that were already underway. Verve Energy also considered that any amendments should not apply to Reserve Capacity Cycles where the certification process was complete.

No other issues with the practicality of implementation were identified.

The IMO's decision

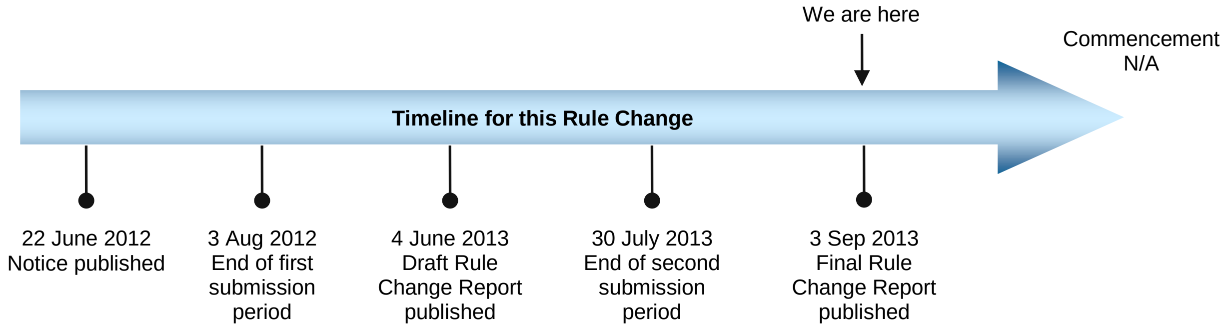
The IMO's decision is to reject the Rule Change Proposal.

1. Rule Change Process and Timetable

On 14 June 2012 Synergy submitted a Rule Change Proposal regarding amendments to clause 4.1.26 of the Wholesale Electricity Market Rules (Market Rules).

This proposal is being processed using the Standard Rule Change Process, described in section 2.7 of the Market Rules. In accordance with clause 2.5.10 of the Market Rules, the IMO decided to extend the timeframes for the preparation of the Draft Rule Change Report, the second submission period and the preparation of the Final Rule Change Report. Further details of the extensions are available on the Market Web Site: http://imowa.com.au/RC_2012_10.

The key dates in processing this Rule Change Proposal, as amended in the extension notices, are:



2. Proposed Amendments

2.1. The Rule Change Proposal

The Reserve Capacity Mechanism requires credited capacity to be available from the first day of the Capacity Year (1 October). To ensure that new capacity arrives prior to this date the window of entry for new capacity was brought forward via the Rule Change Proposal: Changing the Window of Entry into the Reserve Capacity Mechanism (RC_2009_11[1]) from 1 August – 30 November to 1 June – 30 September. Synergy considered that, as a result of RC_2009_11, the market had recognised that conventional generation, as opposed to Demand Side Programmes (DSPs), was prone to being unreliable for several months after commissioning. The change in the timing for entering the market, which provided Market Participants with access to an earlier stream of Capacity Credit payment, was to reduce the risk that generation capability would be late entering the market and thus require the IMO to acquire supplementary capacity.

Synergy also considered that there is a technical difference between generation capacity and other forms of capacity such as DSPs and that this difference serves as a basis on which to differentiate access to early capacity payments. That is, access to the early capacity payments should only be available to conventional generators and not to forms of capacity which do not suffer extended periods of post commissioning remedial work which could materially affect their reliability.

Synergy consequently proposed amendments to clause 4.1.26 of the Market Rules to limit early

[1] Further details are available on the Market Web Site: http://www.imowa.com.au/RC_2009_11.

capacity payments between 1 June and 30 September to Scheduled Generators and Non-Scheduled Generators only. Other capacity types, such as DSPs would only be entitled to capacity payments from 1 October when their Reserve Capacity Obligations begin to apply.

For full details of the Rule Change Proposal please refer to the Market Web Site: http://www.imowa.com.au/RC_2012_10.

2.2. The IMO's Initial Assessment of the Rule Change Proposal

The IMO decided to progress the Rule Change Proposal to allow interested parties an opportunity to provide submissions as part of the rule change process.

2.3. Request for views on complete removal of early capacity payments

In the Rule Change Notice, the IMO considered that after two years of providing access to early capacity payments for new entrants it was now appropriate to reconsider the ongoing need for maintaining this incentive structure. The IMO noted that RC_2009_11 was implemented during a time of capacity shortage in the market, when the benefit of encouraging the timely delivery of capacity was considered likely to exceed any potential costs to the market. The IMO suggested that it was appropriate, now that better cost information was available, to review this assessment, particularly given the fact that other incentives exist or are currently under consideration.

On this basis the IMO sought the views of interested parties on extending the concept presented in the proposal to remove early capacity payments in their entirety, for both generation and demand side options.

3. Consultation

3.1. The Market Advisory Committee

June 2012 Meeting

The Pre Rule Change Proposal was discussed by the Market Advisory Committee (MAC) at the 13 June 2012 meeting. The following points were raised during the discussion:

- Mr Corey Dykstra noted his support for the proposal on its merits. He added that focusing on market outcomes would create a need to treat different types of capacity differently. He added that early capacity payments did not incentivise generators to be available early; instead the penalties associated with not being available early are the more significant incentive. Mr Wayne Trumble concurred that the other incentives in the market such as capacity refunds applying after 1 October will drive a generator to enter the market on time.

- Mr Michael Zammit said that the Rule Change Proposal would be more appropriate in the Reserve Capacity Mechanism Working Group (RCMWG) which is dealing with Demand Side Management (DSM) comprehensively. He added that DSPs should be given a chance to present their own analysis and point of view and that if early registration was removed universally, then his organisation might support it.

- The Chair noted that when a similar proposal from Alinta to remove the ability of DSM to get early entry capacity payments (PRC_2010_30) was considered by the MAC, the IMO had noted that approving the change would require clearly illustrating that the proposed change would not be discriminatory in nature (Wholesale Market Objective (c)). The Chair noted that it had sought advice on Alinta's proposed amendments and whether they would be discriminatory from Marchment Hill Consulting[2].

- Discussion ensued on whether there were features of DSM that make it different from generation. The Chair noted that from a technical perspective there might be a difference but that should not translate to treating them different commercially. Mr Will Bargmann noted that Synergy had legal advice on the discriminatory nature of the proposed rule amendment and was happy to share it with the MAC. *Note: a copy of Synergy's legal advice dated 13 June 2012 was distributed to MAC members at the 11 July 2012 meeting and an electronic copy circulated by email on 26 July 2012.*

The MAC agreed that the Rule Change Proposal should be submitted into the formal process.

<u>August 2012 Meeting</u>

A concept paper from Synergy on the cost and benefit trade-offs of early capacity payments was presented at the 8 August 2012 MAC meeting[3]. The following points were raised during the discussion:

- Mr Stephen MacLean noted that there had been some discussion during the 13 June 2012 MAC meeting as to whether it might be appropriate to remove the early entry payments in their entirety. Mr MacLean noted that there were other options for consideration with respect to the wider question around the continued appropriateness of early entry capacity payments.

- The Chair noted that the need to incentivise the early entry of capacity can depend on the capacity situation in the market at that time. The original rule change that amended the entry period had been progressed when the market was experiencing a shortage of capacity and a potential supplementary capacity event. The capacity situation in the market is now markedly different.

- Mr MacLean advised that Synergy had identified option C[4] as the most likely to be agreeable to MAC members. Mr MacLean stipulated that option C entailed the IMO assessing and making the decision as to whether early capacity payments were required potentially a year before the capacity is required.

- Mr Ben Tan noted his concern that signaling the applicability of early capacity payments a year before would be too late for a Market Generator to adjust its commissioning schedule. The Chair noted that transparency of the criteria applied by the IMO would allow potential investors the relevant information to determine whether it was likely that early capacity payments would apply. Mr Tan indicated his support with installing some flexibility but noted that financiers like simple clear-cut concepts. Mr Tan indicated his support for a

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[2] Marchment Hill Consulting's advice to the IMO is available in the papers for the December 2010 MAC meeting: http://www.imowa.com.au/MAC_34

[3] Synergy's concept paper (CP_2012_02) is available on the Market Web Site: http://imowa.com.au/concept-papers.

[4] Option C gave the IMO the discretion to review the status of existing capacity and the need for new capacity in the coming Capacity Year and so determine whether there is sufficient value to the market in offering an early capacity payment or not.

mechanism to be in place with which the IMO had the responsibility to make a decision, however, the decision needed to be made as soon as possible by the IMO so as to provide the appropriate signals to the market to bring forward the entry of capacity into the market.

- Mr Patrick Peake noted that the original concept of the window of entry had been included in the Market Rules to ensure that Commissioning Tests of various facilities were spread out; thereby ensuring System Management had the capacity to enable required testing prior to the hot season. Discussion ensued as to the complexities of commissioning various types of capacity and whether it would be more appropriate to target supplementary capacity costs specifically to a facility that causes the event that was late in undertaking commissioning.

- Mr David Murphy noted that this issue seemed to be a fundamental market policy issue rather than an operational issue and suggested that the Public Utilities Office (PUO) should further consider whether a policy direction would be appropriate. Mr Murphy noted that a robust long term solution was needed. The Chair acknowledged Mr Murphy's comment that the PUO had offered to take on this matter and suggested that the PUO report back to the MAC at the September 2012 meeting with some preliminary feedback and timelines for its consideration of the wider issue of incentivising early entry of capacity. Mr Murphy noted that the PUO would consult further with the MAC in determining a policy direction.

September 2012 Meeting

During the 12 September 2012 MAC meeting, the Chair noted that Mr Murphy had provided him with an update of the status of the PUO's consideration of the issue of incentivising early entry capacity. In particular, the PUO had determined it would be most appropriate to await the outcomes of the RCMWG. Mr Murphy noted that the PUO did not want to provide any sort of policy direction that could potentially be inconsistent with the outcomes of the RCMWG. Mr MacLean noted his concern with this approach.

Further details are available in the MAC meeting minutes available on the Market Web Site: http://www.imowa.com.au/MAC

Update of events following the September 2012 MAC Meeting

The final meeting of the RCMWG was held on 28 February 2013 and the outcomes of its work reported to the MAC at its 20 March 2013 meeting. While the working group did not specifically consider options for early capacity payments its outcomes included general agreement to:

- continue to regard capacity in the WEM as being a single product, rather than develop a range of different capacity products; and

- progress a number of changes to the Market Rules to harmonise the treatment of DSM and generation capacity by increasing the availability and performance requirements for DSPs.

On 8 May 2013, the PUO confirmed that the IMO should continue to progress RC_2012_10 and its counter-proposals. The IMO received no policy direction in relation to the early entry of capacity into the WEM.

3.2. Submissions received during the first submission period

The first submission period for this Rule Change Proposal was held between 25 June 2012 and 3 August 2012. Submissions were received from APA Group, Community Electricity, EnerNOC, Griffin Energy, Perth Energy, Synergy and Verve Energy.

APA Group, Community Electricity, Perth Energy, Synergy and Verve Energy supported the Rule Change Proposal, agreeing with Synergy's view that DSPs did not have a summer peak period arrival risk due to their less complex commissioning requirements and therefore did not require a financial incentive to enter the market early. Community Electricity also suggested that unlike DSM capacity, generation capacity was capital intensive and developers needed to service their debt as soon as the station is commissioned. APA Group and Verve Energy reiterated Synergy's submission in its Rule Change Proposal that the amendments implemented by RC_2009_11 were aimed at generation capacity only and their application to DSM capacity was the result of an oversight.

Perth Energy further considered that there should be no payment to DSM capacity as "generation" capacity under any circumstances.

EnerNOC and Griffin Power did not support the Rule Change Proposal. EnerNOC considered the proposal is based on flawed assumptions and seeks a retroactive change which discriminates against one class of capacity provider. EnerNOC also questioned the relevance of Synergy's legal advice to the main technical arguments outlined by Synergy.

Griffin Power noted the RCMWG's recent decision not to define "generation" capacity and "non-generation" capacity separately. As "Certified Capacity" had been broadly defined as any marginal MW of energy (produced or shed), Griffin would not support a proposition that one form of capacity be treated differently from another form, despite the legal interpretation supplied by Synergy.

None of the submitting parties expressed support for the complete removal of early capacity payments, apart from Synergy who considered it one of a number of options worthy of further consideration. There was however wider support for changes to remove early capacity payments during times of excess capacity, although specific details of the criteria for allowing the payments for a Reserve Capacity Cycle and the timeframe for making such decisions were not provided. EnerNOC recommended that the whole issue of the timing of entry of new Facilities be considered by the RCMWG as part of its holistic review.

Verve Energy and EnerNOC both considered that in order to avoid undue regulatory risk the proposed changes should not apply to Reserve Capacity Cycles for which the certification process is complete.

The assessment by submitting parties as to whether the proposal would better achieve the Wholesale Market Objectives is summarised below:

Submitter	Wholesale Market Objective Assessment
APA Group	The proposal will better facilitate Wholesale Market Objectives (a), (b) and (d) and on balance better achieves the Wholesale Market Objectives. Noted Synergy's legal advice and considered that even if the proposed amendments contravene Wholesale Market Objective (c), this should not carry greater weight than the

Submitter	Wholesale Market Objective Assessment
	benefits it brings to the market through the effect on Wholesale Market Objectives (a), (b) and (d).
Community Electricity	Improves achievement of Wholesale Market Objective (d) and is consistent with the remaining Wholesale Market Objectives (even being "harmonious" with Wholesale Market Objective (c)).
EnerNOC	Slightly negatively impacts on Wholesale Market Objective (a), negatively impacts on Wholesale Market Objectives (b), (d) and (e) and strongly negatively impacts on Wholesale Market Objective (c).
Griffin Energy	No assessment provided.
Perth Energy	Better facilitates achievement of Wholesale Market Objectives (c) and (d). Any inconsistency that may be perceived with Wholesale Market Objective (c) would be far outweighed by the positive benefit flowing from Wholesale Market Objective (d). No other impacts on the remaining Wholesale Market Objectives identified.
Synergy	Supports Wholesale Market Objectives (a), (c) and (d) and is not inconsistent with Wholesale Market Objectives (b) and (e).
Verve Energy	Agreed with Synergy's assessment of the impact on the Wholesale Market Objectives. Further considered that, should the IMO adopt Verve Energy's suggestion for a more dynamic early entry capacity payment mechanism, the impact on the Wholesale Market Objectives, as outlined by Synergy, is further strengthened.

A copy of all submissions in full received during the first submission period is available on the Market Web Site: http://www.imowa.com.au/RC_2012_10.

3.3. The IMO's response to submissions received during the first submission period

The IMO's response to each of the issues identified during the first submission period is presented in Appendix 1 of the Draft Rule Change Report, available on the Market Web Site: http://www.imowa.com.au/RC_2012_10.

3.4. Submissions received during the second submission period

Following publication of the Draft Rule Change Report on the Market Web Site, the second submission period was held between 5 June 2013 and 30 July 2013. The submission period was extended by 20 Business Days in response to a request from Synergy. Synergy considered that the matters involved in the proposal were complex and requested more time to understand all elements of the IMO's proposed decision and to undertake necessary consultation in preparing its response.

The IMO received submissions from Alinta Energy, Synergy and Verve Energy. All the submissions supported the Rule Change Proposal, suggesting that early capacity payments for DSPs were an unintended consequence of RC_2009_11 and were unjustified due to the lower commissioning risks of DSPs compared with generators. Synergy contended that the IMO had misinterpreted Synergy's legal advice with regard to indirect discrimination and its application to the proposal.

Alinta and Verve Energy expressed support for the IMO to develop and progress changes to ensure that generators were only entitled to early capacity payments when there was a shortage of capacity. Both parties sought clarification on the IMO's prioritisation of this issue compared with other items in the IMO's Rule Change Log and the Market Rules Evolution Plan.

A copy of all submissions in full received during the second submission period is available on the Market Web Site: http://www.imowa.com.au/RC_2012_10.

3.5. The IMO's response to submissions received during the second submission period

The IMO's responses to each of the issues identified during the second submission period are presented in Appendix 1 of this Final Rule Change Report.

3.6. Public Forums and Workshops

No public forums or workshops were held with regard to this Rule Change Proposal.

4. The IMO's Draft Assessment

The IMO's draft assessment, against clauses 2.4.2 and 2.4.3 of the Market Rules, and analysis of the Rule Change Proposal can be viewed in the Draft Rule Change Report available on the Market Web Site: http://www.imowa.com.au/RC_2012_10.

5. The IMO's Proposed Decision

The IMO's proposed decision was to reject the Rule Change Proposal. The IMO made its proposed decision on the basis of its assessment that overall the proposed Amending Rules are inconsistent with the Wholesale Market Objectives.

6. The IMO's Final Assessment

In preparing its Final Rule Change Report, the IMO must assess the Rule Change Proposal in light of clauses 2.4.2 and 2.4.3 of the Market Rules.

Clause 2.4.2 outlines that the IMO *"must not make Amending Rules unless it is satisfied that the Market Rules, as proposed to be amended or replaced, are consistent with the Wholesale Market Objectives".* Additionally, clause 2.4.3 states, when deciding whether to make Amending Rules, the IMO must have regard to the following:

- any applicable policy direction from the Minister regarding the development of the market;
- the practicality and cost of implementing the proposal;
- the views expressed in submissions and by the MAC; and
- any technical studies that the IMO considers necessary to assist in assessing the Rule Change Proposal.

The IMO notes that there has not been any applicable policy direction from the Minister or any technical studies commissioned in respect of this Rule Change Proposal. A summary of the views expressed in submissions and by the MAC is available in section 3 of this report.

The IMO's assessment is outlined in the following sub-sections.

6.1. Wholesale Market Objectives

The IMO considers that overall the proposed amendments are inconsistent with the Wholesale Market Objectives, with the potential benefits to Wholesale Market Objectives (a) and (d) outweighed by the negative impact on Wholesale Market Objective (c). The IMO is not convinced that the proposed cost and efficiency benefits could not be achieved without targeting a specific type of capacity.

The IMO's assessment is presented below.

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

In times of excess capacity the removal of early capacity payments for DSM facilities would reduce the overall cost of these payments and so improve the economic efficiency of the market. However, in times where a capacity shortfall is possible any potential savings could be significantly outweighed by the associated risks to system reliability and the potential need to seek supplementary capacity.

The IMO notes that there is no guarantee that a new DSP will enter the market in time for the start of the Hot Season. Historically, not all new DSPs have met the start date or even the end date of their relevant entry window (originally 1 August – 30 November and now 1 June – 30 September).

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

The proposed amendments may slightly discourage the entry of new DSM facilities, but no material impact would be expected.

(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.

In general, the IMO does not consider the different treatment of different facility types to be discriminatory (in the context of Wholesale Market Objective (c)) where it is *necessary* due to the technical characteristics of the facilities. Examples of this include the different methodologies needed to determine Certified Reserve Capacity for Scheduled Generators, Intermittent Generators and DSPs, and the different dispatch arrangements for Scheduled and Intermittent Generators.

There is however no evidence to suggest that the removal of early capacity payments for DSPs is *necessary* on technical grounds. Rather it has been suggested that it might be possible for the market to pay less for the timely entry of new DSPs into the market due to their lower capital costs and risk profiles, despite the value of the service provided (capacity) being the same as that provided by the timely entry of a new generator.

Even where the different treatment of facility types is not required on technical grounds, it may not be discriminatory if no facility type is disadvantaged or denied an opportunity as a result. An example of this is the restriction of early certification under clause 4.28C.1 to new generating systems. This restriction does not disadvantage other capacity types as they are extremely unlikely to have project lead times that cannot be accommodated within the normal Reserve Capacity

Cycle timeframes, and so would gain little benefit from early certification. (The IMO notes that it has not received any applications for Early Certified Reserve Capacity to date.)

Again however this is not the case for the proposed amendments, which would clearly disadvantage providers of DSM capacity.

The IMO notes that Synergy's legal advice also lists a number of differences between DSPs and generators, for example in terms of licensing requirements, registration requirements and variations in the Market Rules around availability and dispatch obligations. The advice suggests that in the context of these differences the current capacity payment mechanism may amount to indirect discrimination, in that simply applying the same basis of compensation (capacity payments) does not take sufficient account of the significant differences between DSPs, Scheduled Generators and Non-Scheduled Generators.

The IMO agrees that the application of the same rules to different facility types may occasionally result in indirect discrimination. However, Synergy's legal advice does not explain how the differences listed create a difference in the value provided by a DSP or a generator in return for early capacity payments, namely the timely provision of new capacity to prevent a capacity shortfall, which risks system reliability and creates a need to acquire supplementary capacity. It is difficult to see how a DSP receiving the same payment for providing the same service constitutes indirect discrimination against generators.

For these reasons the IMO considers that the proposed amendments discriminate against DSM technology options and so would have a strong negative impact on Wholesale Market Objective (c).

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

While the proposed amendments may reduce costs by avoiding early capacity payments for new DSM capacity, the potential savings would need to be balanced against the risk of increased costs due to the need to acquire supplementary capacity in the event of a capacity shortfall.

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

The proposed amendments may slightly discourage the use of DSM technologies that work to reduce consumption at times of peak demand, but no material impact would be expected.

6.2. Practicality and Cost of Implementation

The IMO has not identified any additional costs associated with the implementation of the Rule Change Proposal.

EnerNOC identified a significant negative financial impact, in excess of $1 million, if the amendments were implemented as proposed and affected Reserve Capacity Cycles that were already underway. Verve Energy also considered that any amendments should not apply to Reserve Capacity Cycles where the certification process was complete.

No other issues with the practicality of implementation were identified.

7. The IMO’s Decision

The IMO’s decision is to reject the Rule Change Proposal.

7.1. Reasons for the decision

The IMO made its decision on the basis of its assessment that overall the proposed Amending Rules are inconsistent with the Wholesale Market Objectives.

7.2. Alternative changes to the incentives for early entry of new capacity

Although the IMO’s decision is to reject this Rule Change Proposal, the IMO acknowledges the concerns raised by stakeholders around the costs of early capacity payments to the market. The IMO also notes that Synergy and other stakeholders have proposed a number of alternative options to provide for a better cost-benefit trade-off for early capacity payments.

The submissions received expressed little support for the complete removal of early capacity payments. However, several of the submissions received in the first and second submission periods expressed support for changes to remove early capacity payments for all facility types during times of excess capacity, although specific details of the criteria for allowing the payments for a Reserve Capacity Cycle and the timeframe for making such decisions were not provided. Further work would be required to assess whether this option provided the best net benefit to the market, and if so to determine the appropriate decision criteria and timeframes. The IMO has accordingly included this issue in its Rules Suggestions Log for future consideration.

Appendix 1. Responses to Submissions received during the second submission period

	Submitter	Comment/Change Requested	IMO's Response
1.	Alinta Energy	There are differences in the characteristics of generation and DSM which mean that the commissioning risk of DSM capacity is not as high. RC_2009_11 was intended to incentivise early entry of capacity to ensure that any post-commissioning further refinements to operation could be undertaken before the Hot Season. DSPs are however not exposed to the post-commissioning reliability issues of a generator.	RC_2009_11 gave two arguments for changing the entry window for new capacity. The proposal noted that "by coming on no later than 1 October new plant will have a few months to fine-tune its operations before the summer peak demand period". However, the IMO also considered that the existing entry window might encourage a developer to take an unreasonably optimistic view when targeting the existing 30 November deadline, increasing the risk of the facility not being available at all by the start of the Hot Season. Overall, the purpose of early entry capacity payments is to incentivise the timely delivery of reliable capacity, to avoid potential capacity shortfalls and the need for supplementary capacity. Delays in the delivery of reliable capacity are not only due to post commissioning reliability issues, but can also be due to issues that arise during the development and commissioning of a facility. See also the IMO's response to issue 4.
2.	Synergy	Allowing access to early capacity payments was designed as an incentive for new plant to commission ahead of the Capacity Year to provide an extended period to achieve reliability and for System Management to schedule the required testing prior to the peak load season of summer. In effect, it acts as a carrot for new plant to commission early to address the almost inevitable post commissioning issues (especially in respect of large thermal plant).	Please refer to the IMO's response to issue 1.
3.	Verve Energy	RC_2009_11 was intended to encourage new Facilities to enter the market as early as possible, with any subsequent	Please refer to the IMO's response to issue 1.

	Submitter	Comment/Change Requested	IMO’s Response
		delays in commissioning and/or unplanned outages being less likely to affect the security and reliability of the power system over the summer period when demand reaches system peaks.	
4.	Synergy	It is appropriate to differentiate access to early capacity payments because the DSP commissioning process deals with communication and load control technologies for existing loads whereas the commissioning process for new generation plant deals with the integration of a large range of technologies and processes that typically result in an extended fault resolution period post commissioning. Synergy maintains that these technical differences resolve to markedly different risk profiles, in regard to the extent that they can impact system reliability and security during the summer peak season and therefore the need to initiate an SRC event. In short, a four month reserve capacity window is considered not to be required for new load based capacity.	While the commissioning of a DSP may be simpler than the development of a baseload generator, it is still typically a multi-step process with numerous complexities and dependencies, particularly for programmes involving multiple loads. The changes proposed in the Rule Change Proposal: Harmonisation of Supply-Side and Demand-Side Capacity (RC_2013_10) are expected to further increase the commissioning requirements for DSPs. As such there is a real risk that a new DSP may not be available by the start of the relevant Hot Season. Further, the value to the market of timely capacity delivery (in terms of avoiding capacity shortfalls and the need for supplementary capacity) depends on the quantity of reliable capacity delivered, not the cost, complexity or risk of its commissioning. For example, in times of tight supply the timely arrival of a 50 MW DSP will contribute to reducing the need for supplementary capacity no differently to the timely arrival of a 50 MW generator.
5.	Verve Energy	The risk profile associated with commissioning Scheduled or Non-Scheduled Generators differs materially to that of DSM. This is principally because capacity provided by DSM is typically provided by existing loads, and so would not be expected to require an extended period to ensure they are commissioned. Even if the loads were not existing loads, Verve Energy considers it unlikely that the capacity provided would represent a risk to the security and reliability of the power system over the summer period.	Please refer to the IMO’s response to issue 4.

	Submitter	Comment/Change Requested	IMO's Response
		There are some "activities" that DSM Facilities may need to complete in order to ensure readiness (for example, installing and testing telecommunications equipment). However, Verve Energy does not consider these "activities" to be comparable to the activities required to commission a thermal generation plant, for example.	
6.	Alinta Energy	Alinta does not consider contracting (for Associated Loads) should be treated as a commissioning activity for the purposes of the IMO's assessment of whether DSM has a summer peak arrival risk. For a DSP any contracting of Associated Loads should have occurred prior to its commissioning activities; including contracting into any list of commissioning activities is equivalent to including "building of turbines" onto the list of commissioning activities for a generator. Until there is a facility constructed (which for a DSP requires having put contracts in place) there is in essence no facility to commission. While not having a facility built in the first place is a risk to the system, mitigating this risk is not the intention of early entry capacity payments. Rather it should be mitigated through the IMO's certification process.	Whether the contracting of Associated Loads should be regarded as a "construction" or a "commissioning" activity is open to debate. However as noted previously, the timely arrival of reliable new capacity can be threatened as much by delays in a "construction" phase as by delays in a commissioning or post-commissioning phase. The IMO does not therefore consider there is any justification to exclude consideration of construction risks in any assessment of risk profiles.
7.	Alinta Energy	It is questionable whether the value of DSM capacity during a short supply situation is in reality exactly the same as that provided by traditional generation assets due to differences in their performance drivers. Alinta suggests that the IMO seeks System Management's advice on the differences between the commissioning activities of a generator and a DSP, and the associated risks to system security and reliability.	The IMO has not been presented with any evidence demonstrating that the value of DSM capacity in a short supply situation is less than the capacity value provided by a generator. System Management has indicated that to date DSPs have been successful in responding to Dispatch Instructions and delivering their capacity to the market when required. Please also refer to the IMO's response to issues 4 and 6.
8.	Alinta Energy	During the consultation processes for RC_2009_11 there was no discussion that DSPs or other non-generation capacity should be entitled to enter the market early and receive capacity payments. This was an oversight at the time which	The IMO considers that although there was no specific discussion regarding DSM as part of RC_2009_11, this does not mean that the Amending Rules would have been different if such a discussion had taken place.

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		has unintentionally resulted in new entrant DSM receiving approximately $9 million of early entry capacity payments since the 2011/12 Capacity Year despite there being a current over-supply of capacity.	From market start all new Facilities were eligible for two months of early capacity payments (for August and September). RC_2009_11 was progressed in response to a capacity shortfall that resulted in the IMO needing to seek supplementary capacity. In this climate it is unlikely that the IMO would have chosen an option that actively discouraged any type of capacity (including DSM capacity) from aiming to enter the market earlier. The IMO notes that several new generators have also entered the market and received early entry capacity payments (despite an over-supply of capacity) since the commencement of the Amending Rules for RC_2009_11.
9.	Synergy	The focus of RC_2009_11 was on providing additional time for Scheduled Generators and Non-Scheduled Generators to work through their commissioning issues such that they achieved satisfactory reliability levels prior to the summer peak season. The RC_2009_11 discussion did not extend to consideration of other forms of capacity because such capacity is, in most cases, procured from existing loads and commissioning of the adjunct technology and equipment is a trivial exercise in comparison with that related to commissioning new Scheduled Generators and Non-Scheduled Generators, leading to the conclusion that access to an extended reserve capacity window is unnecessary for the other forms of capacity. Thus it was an unintended outcome of RC_2009_11 that it also applies to such other forms of capacity and that this oversight in the rules exposes customers to potential additional cost without commensurate benefit.	Please refer to the IMO's responses to issues 1 and 8.
10.	Verve Energy	It is Verve Energy's opinion that Scheduled or Non-Scheduled Generators are the participants who face the risk of commissioning delays that may impact the security and reliability of the power system over the summer period, and therefore these are the participants to whom the Amending	Please refer to the IMO's responses to issues 1 and 8.

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		Rules for RC_2009_11 were intended to apply.	
11.	Synergy	It is efficient to differentiate access to early capacity payments because precluding new load based capacity's access to early capacity payments reduces excess capacity costs imposed on customers in the preceding year noting that the value of excess capacity to customers is negligible.	Please refer to the IMO's assessment against Wholesale Market Objective (a) in section 6.1 of this report. The IMO further notes that in conditions of excess capacity the benefits to the market of the early entry of a generator (unless it fills some specific niche in the market) could also be insignificant compared with the costs.
12.	Synergy	Synergy contends that the IMO has misinterpreted Synergy's legal advice with regard to indirect discrimination and its application to the proposal. The advice supports the proposition that treating capacity technologies the same, which in the context of the proposal is taken to mean access to early capacity payments, represents indirect discrimination favouring one group of capacity technologies, i.e. load based capacity over generation technology based capacity. Synergy notes the IMO, in its assessment, states that Synergy's legal advice does not, in the context of the listed different treatment of technologies, distinguish a value difference between the technologies in providing timely capacity. Synergy holds that this is an incorrect interpretation of the purpose of the advice; it did not seek to draw such a distinction as related to differing capacity technologies in regard to providing a reserve capacity service, rather it defined the nature of indirect discrimination and in treating sufficiently different technologies the same an argument could be made that to do so would amount to indirect discrimination.	The IMO does not agree that it has misinterpreted Synergy's legal advice. In particular, the IMO agrees with Synergy that its legal advice does not seek to distinguish between different technologies in terms of the value of their "timely capacity" service to the market. However, the IMO's point is that it considers such a distinction would need to be drawn in order to justify the different treatment of DSPs in this regard. To do otherwise would effectively penalise a technology for being able to provide a particular service more easily than another technology. This would be similar to paying two generators different energy prices because one could produce energy more efficiently than the other.
13.	Synergy	Synergy agrees with the IMO's position that prolonged delays in attaining commercial operation and therefore commissioned status by new generation capacity may require the IMO to step in and initiate an SRC. However, Synergy does not support the proposition that this conclusion equally applies to DSP	Please refer to the IMO's response to issue 4. The IMO notes that in times where capacity is in short supply, any portion of the certified capacity of a new DSP that was not delivered on time would contribute to

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		capacity. This is because typically a DSP is comprised of a number of Associated Loads of which the aggregator will seek to commission as many as possible prior to mandatory Reserve Capacity Obligations taking effect. The diversification inherent in DSP capacity thus presents a different and lower risk to system reliability and security when compared to a generator of equivalent capacity and therefore does not present an equivalent risk in respect to the need for initiating an SRC event.	the risk of an overall capacity shortfall, while any capacity that was provided would work to reduce the risk of an overall shortfall and the need for supplementary capacity.
14.	Verve Energy	In its Draft Rule Change Report, the IMO noted stakeholders' suggestions for alternative options which may provide for a better cost benefit trade-off for early capacity payments. The IMO noted that it had added this issue in its Rules Issues Log for future consideration. Verve Energy requests clarification from the IMO as to the relative priority of this issue against the other issues on the Rules Issues Log and the Market Rules Evolution Plan.	The proposal to remove early entry capacity payments for all facility types during times of excess capacity has been assigned a "medium" priority in the IMO's Rules Suggestion Log. The IMO intends to provide an update to the MAC on the Market Rules Evolution Plan later this year. This will provide MAC members with an opportunity to suggest additional items for inclusion in the plan and their relative priority. Stakeholders are also able to develop concept papers or Pre Rule Change Proposals for presentation to the MAC on issues they consider are of particular concern.
15.	Alinta Energy	Alinta supports the IMO in developing and progressing changes to the availability of early entry capacity payments to ensure that generation assets are only entitled to these payments where there is a shortage of capacity. Alinta however requests further details of the relative priority of this work compared to other items on the rule change log and Market Rules Evolution Plan from the IMO.	Please refer to the IMO's response to issue 14.
16.	Verve Energy	In its Draft Rule Change Report, the IMO noted that EnerNOC had identified a negative financial impact of $1 million if the amendments were implemented as proposed. However, Verve Energy notes that the negative financial impact identified by Synergy in its Rule Change Proposal of $2.3 million for 2011	The negative financial impact noted by EnerNOC related to Reserve Capacity Cycles for which the certification process was complete and was considered by the IMO to be a potential implementation issue. The IMO notes that Verve Energy agreed with EnerNOC that any

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		and in excess of $8 million for 2012 was not specifically discussed. While these costs have already been incurred, they represent a significant additional cost to the market.	amendments to the Market Rules should not change the arrangements for capacity that was already certified. Significant early capacity payments have been made to both DSPs and generators since the implementation of the Amending Rules for RC_2011_09. However, these payments were not mentioned in section 5.2 of the Draft Rule Change Report as they had no relevance to the "practicality and cost of implementation" of the Rule Change Proposal. The IMO noted the potential cost savings of avoiding early capacity payments to DSPs in times of excess capacity in its assessment of Synergy's proposal against the Wholesale Market Objectives in section 5.1 of the Draft Rule Change Report.