



Agenda Item 9a: Reserve Capacity Security

1. BACKGROUND

When a Market Participant has committed to the development of a new Facility, or a Facility upgrade, the Wholesale Electricity Market Rules (Market Rules) require the Market Participant to provide Reserve Capacity Security in respect of the Facility. This security is required after either:

- the Bilateral Trade Declaration for the Facility is made – if the Market Participant indicates that it intends to bilaterally trade the Certified Reserve Capacity (CRC) associated with the Facility; or
- at the time the Reserve Capacity Auction Offer for the Facility is made – if the CRC is to be offered into the Reserve Capacity Mechanism through the Reserve Capacity Auction process.

Currently the IMO holds in excess of \$24 million dollars in Reserve Capacity Security.

Clause 4.13.10 of the Market Rules outlines that the Reserve Capacity Security is no longer required once:

- The Reserve Capacity Obligations commence; and
- The Facility has operated at 100% of its Reserve Capacity Obligation Quantity (RCOQ) for one Trading Interval within the Reserve Capacity Year. In this case the requirement ceases immediately, subject to a processing period; or
- The Facility has demonstrated that it has operated to a level of at least 90% (but not 100%) of its RCOQ within the Reserve Capacity Year. In this case the requirement ceases following the end of the Reserve Capacity Year.

Note: if the Facility has an RCOQ of zero, the Reserve Capacity Security is to be returned at the end of the Reserve Capacity Year.

If a Facility fails to satisfy the obligations specified in clause 4.13.10 during the Reserve Capacity Year the Reserve Capacity Security is first used to fund any Supplementary Reserve Capacity required in that year, with the remainder distributed to Market Customers proportional to their IRCR level.

2. ISSUES

After a comprehensive review of the administration of Reserve Capacity Security a number of issues with the process have been identified. These issues have been further highlighted as new and diverse facilities have begun commissioning and started to participate in the Wholesale Electricity Market (WEM). Additionally, the recent failure of some Market Participants to meet their obligations has brought these issues to the forefront.

2.1 Provision of Reserve Capacity Security

The IMO has previously required Reserve Capacity Security to be provided by a new Facility or upgrade to an existing Facility only for the first Reserve Capacity Cycle for that Facility.

Following the failure of WA Biomass to enter the market (and therefore meet its obligations) the requirements around the provision of Reserve Capacity Security have been reviewed to ensure that any risks to the market are minimised.

The IMO's review has identified an issue around the lack of clarity regarding the treatment of facilities in subsequent cycles.

- ***How should facilities be treated once their first Reserve Capacity Cycle has lapsed?***

The Market Rules require Reserve Capacity Security to be provided for each Reserve Capacity Cycle until the facility proves it can meet its obligations in respect of the cycle the security has been provided for.

The IMO has previously not required additional security to be provided in subsequent Reserve Capacity Cycles; however the IMO considers that the Market Rules direct the IMO to require Reserve Capacity Security for multiple years.

Given the timing within the current Reserve Capacity Cycle and the associated financial implications, it would seem inappropriate and inconsistent with the previous position adopted by the IMO for Market Participants to be required to provide Reserve Capacity Security for the 2009/10, 2010/11 and 2011/12 Reserve Capacity Years. However, this interpretation of the Market Rules may constitute a Market Rule breach by Market Participants.

The IMO considers that Market Participants should be required to provide adequate Reserve Capacity Security for each Reserve Capacity Cycle from the 2011 Reserve Capacity Cycle onward (2013/2014 Reserve Capacity Year). All Reserve Capacity Security should be released once a facility has performed at the appropriate level the first time (i.e. 90 – 100%).

The IMO will need to ensure that all interested stakeholders are aware of this. A communication plan is set out in section 3 of this paper.

Discussion point 1: Market Participants should be required to provide adequate Reserve Capacity Security for each Reserve Capacity Cycle from the 2011 Reserve Capacity Cycle onward (2013/2014 Reserve Capacity Year).

2.2 Return of Reserve Capacity Security

The majority of issues regarding the return of Reserve Capacity Security are around the treatment of non-conventional generation technologies. In particular, under the current Market Rules different types of capacity providers are treated differently when determining whether to return Reserve Capacity Security (e.g. Intermittent Generators and DSM programmes).

Further consideration of when Reserve Capacity Security is no longer required for each possible type of capacity provider is required to ensure that the Market Rules do not discriminate against non-conventional generation types (Market Objective (c))

The specific issues are as follows:

- ***How should DSM be treated?***

This issue has been considered as part of the Curtailable Loads Concept Paper, also on the agenda for discussion at the May 2010 MAC meeting;

- ***How should Intermittent Generators be treated?***

The current Market Rules can be interpreted as Intermittent Generators, irrespective of actual performance, either:

- automatically receiving security back at the end of a Reserve Capacity year; or
- never being entitled to receive their security back.

Discussion point 2: All Facilities (conventional and non-conventional) should be entitled to receive their Reserve Capacity Security back when they can prove to the IMO that they can perform to the level at which their certification is based.

- ***How should the IMO treat Facility which have been tested and subsequently had their RCOQ reduced?***

The IMO must reduce the number of Capacity Credits assigned to a Facility if it fails a Reserve Capacity Test. Currently these facilities may be entitled to have their full Reserve Capacity Security returned if it has reduced Reserve Capacity Obligations as a result of failing a test. It appears a perverse outcome that a facility which has exposed the market to the potential need to call Supplementary Reserve Capacity could benefit by having its Reserve Capacity Security released.

Discussion point 3: Should a facility be entitled to have its full Reserve Capacity Security returned if it has reduced Reserve Capacity obligations as a result of failing a test.

- ***How early should Facilities be entitled to get their Reserve Capacity Security back?***

Currently a Market Participant can only request the return of its Reserve Capacity Security once the RCOQs apply (e.g. from 1 July in Year 3). Early commissioning of the Facility does not entitle the Market Participant to have its Reserve Capacity Security returned any earlier. Should the security be released before the obligations apply in this case?

Discussion point 4: Should Reserve Capacity Security be released before RCOQs apply when a facility has entered the market early.

2.3 Additional identified issues

The following additional issues associated with the Reserve Capacity Security provisions of the Market Rules have been identified:

2.3.1 Circumstances where there is an upgrade

- ***How should Facility upgrades be treated for the purposes of Reserve Capacity Security?***

A Market Participant will be required to provide security to the IMO when it undertakes an upgrade of an existing facility (clause 4.13.1). However for the purposes to determining whether to return any security it is unclear how the IMO would assess that part of a Facility has performed at the required level (between 90% and 100%) in the circumstances where the upgrade is not independent of the rest of the plant.

For example consider a Market Participant who upgrades its previous 100MW Facility by installing inlet cooling and increasing the output of the facility to 120MW. The upgrade can not be assessed separately from the existing 100MW Facility. Should the required level of output for the return of any Reserve Capacity Security be at:

- 118 MW (the existing 100MW Facility and 90% of upgrade);
- 108 MW (90% of the existing 100MW Facility and 90% of the upgrade); or
- 108 MW (90% of the Facility as a whole)?

Discussion point 5: How should Facility upgrades be treated for the purposes of Reserve Capacity Security.

2.3.2 Cancellation of Capacity Credits

- ***Should the IMO be able to cancel Capacity Credits rather than drawing down on Reserve Capacity Security in the case of a default or failure to build the Facility?***

The failure of WA Biomass to enter the market and deliver the required capacity placed the market at risk as the IMO could not cancel its Capacity Credits. This has also been an issue for other generators who have identified in advance that they will be unable to enter the market in time to meet their obligations.

Discussion point 6: The Market Advisory Committee to note that this issue is currently under consideration by the IMO. A separate paper will be provided on this issue at the June MAC meeting.

3. COMMUNICATION PLAN

The IMO intends to ensure that all interested stakeholders are aware that Reserve Capacity Security will be required for each Reserve Capacity Cycle via the following methods:

- An email will be sent to all interested parties clarifying that Reserve Capacity Security will be required for each Reserve Capacity Cycle and outlining the IMO's intention to propose a rule change to clarify this further in the Market Rules; and
- The IMO will include details of the requirement to provide Reserve Capacity Security for subsequent Reserve Capacity Cycles in any training presentations.

4. RECOMMENDATIONS

The IMO recommends that the MAC:

- **Discuss** each of the issues raised in section 2;
- **Discuss** whether the IMO's intended communication plan will adequately clarify that Reserve Capacity Security will be required for each Reserve Capacity Cycle prior to any Amending Rules taking effect; and
- **Agree** for the IMO to prepare a Rule Change Proposal to resolve the issues.