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Submitted by [redacted] to https://www.erawa.com.au/consultation

15 April 2019,

Australian Energy Market Operator allowable revenue and forecast capital expenditure proposal for 2019/20 to 2021/22

The Australian Energy Council (AEC) welcomes the opportunity to make a submission to the Economic Regulation Authority on the 'Australian Energy Market Operator allowable revenue and forecast capital expenditure proposal for 2019/20 to 2021/22'. The AEC is the industry body representing 23 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia and sell gas and electricity to over 10 million homes and businesses.

The AEC supports an AEMO revenue requirement based on independently determined efficient costs. Considering the early stage of development of the market reform program, we are concerned with the ability to assess the AEMO revenue requirement, given the detail design of the wholesale market and the Information Technology systems required to operate such a market are yet to be identified. In other words, can the allowable revenue be efficiently determined in the absence of a detailed design?

Therefore, the AEC would prefer the ERA take a ***staged approach to funding approval*** (particularly in relation to Capex expenditure), and that AEMO proposes additional funding, as clarity and certainty develops through the market reform program.

Overall, the AEC supports the need for market reform, but we express concern as to the increasing governance and management complexity of WEM operations adding to the cost of market fees. The AEC observes that whilst the WEM market size is small, the market fees are significant and increasing. It is also expected that the market fees will be recovered over a smaller quantity of energy (MWh) as DER uptake increases further. The AEC is concerned that the difficulties of administering an increasingly complex system brought about by the continued growth of DER and the introduction of a constrained access framework will act to further increase AEMO costs and market fees. Therefore, care must be taken not to over invest in market administration and consideration given as to who pays for defining and implementing market reform. In this regard, AEC believes that participant fees should relate to costs of operating the market and accordingly ***market participants should not pay for government led market reform***. In effect, consumers are being asked to pay upfront for reforms without any guaranteed benefits. The $51M capex requirement for reform in the AR5 allowable revenue request is significant.

Funding reform via market fees adds difficulty to AEMO's task of minimising participant fees. The SWIS is a small electricity system and management of it needs to focus on fit for purpose solutions that remain cognizant of the fact that costs are recovered from relatively small volumes. On an energy basis, the WEM is 10% of the size of the NEM and market fees are approximately twice that of the NEM ($0.791/MWh compared with $0.410/MWh – FY18[1]). In absolute dollar terms, the WEM budget is proportionately high - approximately 36%

of the NEM in FY19 ($30.3m compared with $83.4m[1]). Additional costs budgeted by AEMO to navigate the reform process will place unreasonable burden on market participants, which will ultimately be borne by consumers.

The AEC is also mindful of fee increases being driven by inefficient investment signals in relation to DER, and that consideration be given to how costs caused by DER integration can be better allocated on a **causer pays principle**.

It appears likely that AEMO will be expected to incur additional costs in dealing with operational complexity caused by increased connection of Distributed Energy Resources (DER). A recent AEMO report suggests this complexity is set to increase in the short-term and Recommendation 4 - WEM Reform Program additional scope and focus[2]; calls for "Additional scoping of the objectives and timelines of the reform program is necessary to include mechanisms for DER integration in the detailed design in a timely manner." The AEC observes that DER resources are causing increased costs in system management, for which market participants (and ultimately consumers) are paying.

Given the reform agenda and increasing system complexity leading to AEMO fee increases the AEC suggests there may be benefit in the ERA reviewing the way AEMO's costs are recovered from market participants in future (and potentially from non-market participants). An alternative fee allocation methodology that considers the causer pays principle may be worthwhile investigating given the high quantum of fees in the WEM and the possibility of further increases. We provide in appendix 1 an example of an alternative fee allocation method as used in the National Electricity Market. This isn't to say the NEM method is best suited to the WA context but simply to stimulate further thinking on the topic.

The AEC also sees a need to consider the effects of inefficient DER investment signals leading to greater DER uptake and how this feeds back to AEMO market fees. There are a number of inefficiencies driving DER uptake that would benefit from further consideration as to how costs of integrating DER are allocated, for example, there is:

1. Inconsistency between the Renewable Energy Buyback Scheme (REBS) pricing and the Balancing Market price
2. Over stimulation of DER investment due to retail tariff design
    a. Under flat rate tariff design solar customers don't pay their share of fixed system costs
3. Over stimulation of DER investment due to the addition of the Tariff Equalisation Contribution (TEC) to the network tariff
    a. This leads to the ability for some consumers to avoid (or proportionately reduce) this charge and leads to non-solar customers paying a greater share of the TEC
4. An inherent unfairness in that whilst behind the meter generation is contributing significantly to the need for the major projects behind AEMO's large expenditures, the structure of WEM participant fees results in these customers largely escaping contribution to these costs.

The AEC believes structure and methodology of ***market fee allocation should be considered*** as part of the market reform program.

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[1] All figures taken from 2018-19 AEMO Final Budget and Fees – June 2018 (https://aemo.com.au/-/media/Files/About_AEMO/Energy_Market_Budget_and_Fees/2018/Final-AEMO-Consolidated-Budget-and-Fees-2018-19.pdf)

[2] INTEGRATING UTILITY SCALE RENEWABLES AND DISTRIBUTED ENERGY RESOURCES IN THE SWIS https://www.aemo.com.au/Electricity/Wholesale-Electricity-Market-WEM/Security-and-reliability/Integrating-utility-scale-renewables

Any questions about our submission should be addressed to Scott Davis, Policy Adviser Western Australia by email to [redacted] by telephone on [redacted].

Yours sincerely,

Scott Davis
Policy Advisor, Western Australia
Australian Energy Council

Appendix 1 - NEM Participant Fee allocation

In determining NEM Participant fees under the National Electricity Rules (NER), AEMO must have regard to the National Electricity Objective (NEO) and the structure must, to the extent practicable, be consistent with the following principles:

- The structure of Participant fees should be simple.
- The components of Participant fees charged to each Registered Participant should be reflective of the extent to which AEMO's budgeted revenue requirements involve that Registered Participant.
- Participant fees should not unreasonably discriminate against a category or categories of Registered Participants.
- Fees and charges are to be determined on a non-profit basis that provides for full cost recovery.
- The structure of Participant fees should provide for the recovery of AEMO's budgeted revenue requirements on a specified basis.

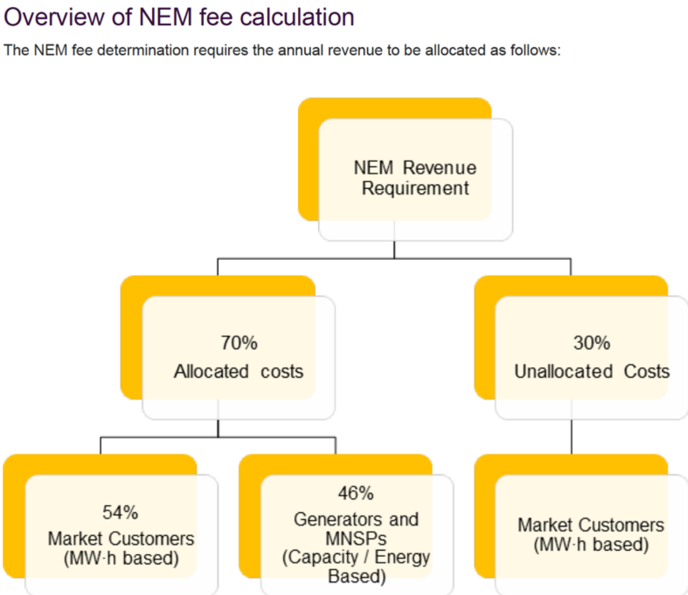

Figure 1 NEM Market Participant Fee Structure[3]

A full description of current cost allocations in the NEM can be found in the 2016 determination of the structure of participant fees[4]. The AEC highlights the following key allocations taken from this report:

Unallocated costs (30%) - relates to common "overheads" in operating AEMO that cannot be allocated to particular categories. In this case the reflective of involvement principle does not provide guidance and therefore AEMO focuses on simplicity and economic efficiency. Allens Consulting Group in their 2010 advice considered the most economically efficient allocation is to recover unallocated costs from end users via the Registered Participants closest to them. AEMO considers the approach of levying unallocated costs on Market Customers via energy charges continues, on balance, to best meet the Rules principles.

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[3] Electricity functions 2018-19 AEMO Final Budget and Fees https://www.aemo.com.au/-/media/Files/Electricity/NEM/Participant_Information/Fees/2018/Final-AEMO-Electricity-Final-Budget-and-Fees-2018-19.pdf

[4] FINAL REPORT - STRUCTURE OF PARTICIPANT FEES IN AEMO'S ELECTRICITY MARKETS 2016 https://www.aemo.com.au//media/Files/Stakeholder_Consultation/Consultations/Electricity_Consultations/Structure-of-Fees/Final-Report--Structure-of-Participant-Fees-in-AEMOS-Electricity-Markets-2016-170316.pdf

Split of Allocated Costs (70%) - AEMO then identified the key broad activities (e.g. power system security, metering and settlements) and allocated NEM direct costs to each of the outputs. Following this, AEMO allocated the activities to categories of Registered Participants based on the 'reflective of involvement' and 'no unreasonable discrimination' criterion and the simplicity principle. This analysis resulted in 46% of direct allocated costs being apportioned to Generators and Market Network Service Providers (MNSPs) and 54% to Market Customers.

Generator and MNSP Fees (46%) - a fully fixed fee was recommended, based half on historic registered capacity and half on historical energy.

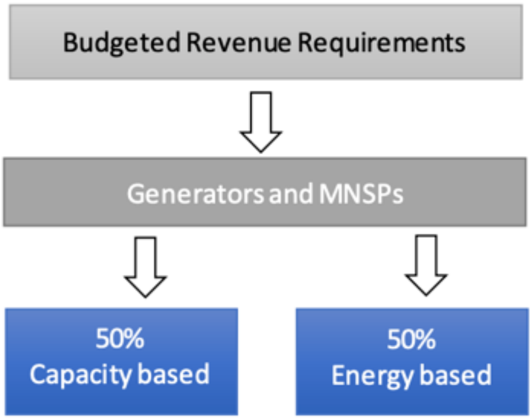

Figure 2 Budgeted Revenue Requirement for Generators and MNSPs[4]

The 2016 structure also recognized that the NEM's Full Retail Competition (FRC) costs were a consequence of the number of customers rather than the size of the customers. To that end, FRC costs were moved in 2016 from an energy-based recovery to a connection-fee recovery.

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