

4 September 2007

Economic Regulation Authority  
PO Box 8469  
Perth BC WA 6849

Dear Sir / Madam

**DISCUSSION PAPER: ANNUAL WEM REPORT TO THE MINISTER**

Thank you for the opportunity to make a submission in respect of the development of the Annual Wholesale Electricity Market (WEM) Report to the Minister. Landfill Gas and Power Pty Ltd (LGP) offers the following comments using the numbering and structure of the Discussion Paper.

**General**

LGP notes the ERA view that in light of the extensive consultation that was undertaken during the restructuring of the electricity industry in Western Australia, and the short time since the WEM has been operating, the ERA considers that the first Minister's Report should be focused on the assessment of the effectiveness of the WEM at a fairly high level. In particular, in the absence of compelling evidence of fundamental problems, the ERA considers that it would be inappropriate to recommend fundamental change in the market at this stage. Further, there is good reason to expect that the WEM will develop as it matures and market participants develop a greater understanding of the operation of the market, and that the rule change process is the appropriate vehicle for facilitating this evolution. LGP's responses to the issues raised in the Discussion Paper are based on this ethos.

**Discussion Point 1:** Given the current WEM design, the ERA invites comment on the extent to which the operation of the Reserve Capacity Mechanism (RCM) is effective in achieving the objectives of the WEM.

LGP supports the ERA's view that a central issue in assessing whether the RCM promotes the objectives of the WEM is the extent to which the RCM has succeeded in promoting new entry required for the efficient, safe and reliable production and supply of electricity. While at the time of issuing the Discussion Paper the ERA noted that the RCM had in fact delivered new capacity investment into the WEM, the recent round of Capacity Certification has emphatically endorsed that view.

**Discussion Point 2:** Bearing in mind the interaction of the capacity market and the energy market, the ERA invites comment on whether the current WEM provides adequate incentives for an efficient mix of generation plant.

Further to the comments in Discussion Point 1, LGP notes that substantial gas and coal fired power stations gained certification in the most recent capacity round, thereby supporting the suitability of the current WEM.

**Discussion Point 3:** The ERA invites comment on whether the WEM adequately promotes efficient location of generation facilities and promotes the efficient development of transmission and distribution networks.

LGP supports the ERA's comments on the central role of the Network Access Offer in locating a generating plant. However, we perceive that Locational Price Signaling ought to contain the further dimension of loss factors, which issue is not addressed in the Discussion Paper. In its current form, the WEM adjusts energy injections and off-takes to take account of network losses. However, it does not apply the same process to certified capacity. LGP perceives that application of loss factor adjustment to certified capacity would further promote the efficient location of generators and loads.

**Discussion Point 4:** The ERA invites comment on whether the WEM adequately promotes investment in an efficient amount of generation capacity.

LGP supports the ERA's position that the short period over which the WEM has been operating does not provide sufficient evidence to judge whether the WEM leads to excess capacity over the long term. In particular, investments in electricity generation are long term, some generation plants are only efficient at significant scales and, as a result, patterns of investment in generation plant tend to be lumpy. This can lead to periods where the supply of capacity is tight, and other periods where there is significant excess capacity.

**Discussion Point 5:** The ERA invites comment on whether there are other issues with the RCM that materially impact on the effectiveness of the WEM.

LGP supports the ERA's preliminary view that any concerns that Rule Participants are likely to be better dealt with through the rule change process.

**Discussion Point 6:** Recognising that the Short Term Energy Market (STEM) is a net pool system, and that the Vesting Contract impacts on liquidity in the market, the ERA invites comment on any aspects of the STEM design that discourage Rule Participants from trading in the WEM.

LGP supports the ERA's position that there is insufficient operating experience upon which to base an informed opinion on the effectiveness of the STEM. In response to the comments in the Discussion Paper proposing the abolition of the STEM in favour of managing the fluctuations of electricity demand via the balancing mechanism, we would reiterate the ERA's comment that the MCAP price is calculated based on the portfolio supply curves from the STEM and that consequently this would seem to not achieve that aim.

**Discussion Point 7:** The ERA invites comment on the day-ahead feature of the STEM. In particular, does the day-ahead feature of the STEM discourage Rule Participants from trading

in the STEM and would introducing two gate closures, or gate closures closer to real time, encourage greater participation? In the event the day-ahead arrangement is replaced by a real-time arrangement or the arrangement where the 'gate closure' time to offer and bid into the STEM is closer to real time events, the ERA invites comment on how the potential exercise of market power by larger participants could be mitigated.

LGP supports the current day-ahead feature of the STEM. We are not aware of any means to encourage higher levels of STEM trading.

**Discussion Point 8:** The ERA invites comment on the effectiveness of the Independent Market Operator (IMO) in carrying out its functions.

LGP supports the comments in the Discussion Paper that the IMO's staff are generally helpful and approachable. In response to the comments in the Discussion Paper:

- i) While LGP regrets the four STEM suspensions, when placed in the context of the design and first year of implementation of a unique market system on a relatively small budget, we consider this to be a small number of suspensions and an indicator of good performance.
- ii) LGP considers the instruction manual to be fit for purpose. In particular, it should be remembered that the manual is supplemented by the real-time availability of experienced IMO operators.
- iii) Noting that audit-ability of invoices is an important function for Rule Participants, LGP agrees that there is a lack of transparency in the IMO invoices. While it is recognised that IMO assistance is readily available in interpreting invoices, it does seem that the IMO itself doesn't have access to the necessary information.
- iv) LGP has participated in all IMO trainings and has found them highly beneficial and well organised.
- v) While LGP does have some issues with the appropriateness of some of what are referred to as the IMO's requirements placed on small Rule Participants, we consider that these requirements are imposed by the Market Rules rather than by the IMO and therefore should not reflect on the effectiveness of the IMO in carrying out its functions. Please see further comment on this issue in the section entitled "Additional Comments."

**Discussion Point 9:** The ERA invites comment on the effectiveness of the System Management in carrying out its functions

LGP supports the general view expressed in the Discussion Paper of satisfaction with System Management.

**Discussion Point 10:** The ERA invites comment on any further steps that could be taken to assist Rule Participants in understanding the Market Rules.

LGP is generally satisfied with the assistance given in understanding the Market Rules; in particular the training and availability and helpfulness of IMO staff.

**Discussion Point 11:** The ERA invites comment on any aspects of the participation of Demand-Side Management (DSM) in the WEM that remain unclear to Rule Participants.

While DSM is an important technique for improving the economic efficiency of the market, LGP perceives it to be impeded by a combination of long lead-times and the requirement for a high educational commitment for participants. In particular, the majority of prospective DSM participants are relatively small and unsophisticated users who need to have the obligations and benefits explained to them and need to see financial outcomes relatively quickly. While LGP does not itself participate in DSM, we would support initiatives to streamline the process for bringing DSM online outside of the formal Capacity Certification process. While this would interfere with the supply/demand balance and impact on the financial structure of Rule Participants, this impact would be relatively minor in comparison to the overall financial and environmental benefits.

**Discussion Point 12:** The ERA invites comment on the adequacy of the existing rule change process. In particular, the ERA is interested in whether or not the current process achieves an appropriate balance between cost, timeliness and transparency.

LGP supports the ERA's position that an appropriate rule change process is an important element of an effective market.

**Discussion Point 13:** The ERA invites comment on any fuel supply constraints faced by Market Participants, and the impact that any such constraints have on the effectiveness of the WEM. In particular, what impact, if any, do fuel supply constraints have on the operation of markets for capacity and energy?

LGP supports the ERA's position that fuel supply problems do not of themselves imply any issues with the effectiveness of the design of the WEM in meeting the market objectives and that addressing gas supply problems is beyond the scope of this review. Nonetheless, we also support the ERA's intention to investigate the impact of gas supply constraints on the operation of the WEM for the purposes of the review.

**Discussion Point 14:** The ERA invites comment on the materiality of the financial impact of consequential outages. The ERA also invites comment on the extent to which participants are able to manage their exposure to consequential outages through commercial arrangements. If participants are unable manage their consequential outages through commercial arrangements, the ERA invites comment on the impact of consequential outages on the effectiveness of the WEM.

LGP is not materially subject to consequential outages. We support the ERA's position that Rule Participants that have entered into contracts that provide for network curtailment should perform the contract. However, in circumstances where there is no such provision, we support the proposition that Rule Participants that are adversely impacted by Consequential Outages outside their control are entitled to a remedy.

**Discussion Point 15:** The ERA invites comment on whether the process for scheduling network outages affects the achievement of the objectives of the WEM.

LGP has no experience of this aspect of the Market Rules but supports the proposition that there is a need to coordinate network outages as well as generator outages.

**Discussion Point 16:** The ERA invites comment on whether the confidentiality of information has impacted on the effectiveness of the WEM and, if so, how?

LGP is not aware of any circumstances in which the confidentiality of information has impacted on the effectiveness of the WEM.

**Discussion Point 17:** The ERA invites comment on whether a more competitive process for the supply of ancillary services would promote the effectiveness of the WEM. In particular, do the current requirements under the Market Rules for an ancillary service contract prevent or deter participants from supplying ancillary services and, if so, how?

LGP would not itself participate in the supply of ancillary services and has no comment on the appropriateness of the current arrangements. However, we would question whether the 'complexity' argument applies in this case; while Rule Participants are adversely affected by any unnecessary complexity in the compulsory features of the market, they can choose to be unaffected by complexity in the esoteric features.

**Discussion Point 18:** The ERA invites comment on any specific events, behaviour or matters (not covered elsewhere in this Discussion Paper) that have impacted on the effectiveness of the market. In particular, the ERA invites comments on any specific events, behaviour or matters that are relevant to the achievement of the objectives set out in clause 1.2.1 of the Market Rules.

LGP notes the ERA's position that the Rule Change Process is available for Rule Participants to address the issue of generators having to pay the cost of meter upgrades.

#### **Additional Comments**

LGP supports the proposition that small Rule Participants should be considered a special case and wherever possible the Market Rules should be relaxed in respect to them. The stated example of exemption from the requirement to use the Austraclear system is well chosen. In addition, it should be noted that small generators in general, and small intermittent generators in particular, have only a minor impact on the system and, further to the above comments on DSM, could reasonably be given less onerous obligations in matters such as capacity certification and availability.

We trust these responses are helpful. If you require further information please contact our General Manager Retail, Dr Steve Gould or myself.

We look forward to the issue of the final paper.

Yours sincerely

**GRAEME ALFORD**  
**CHIEF EXECUTIVE OFFICER**