

18 December 2019

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Submitted online via the ERA portal

Dear Sara

ANNUAL REPORT TO THE MINISTER FOR ENERGY ON THE EFFECTIVENESS OF THE WHOLESALE ELECTRICITY MARKET 2019 - ISSUES PAPER

Thank you for the opportunity to make a submission regarding the Economic Regulation Authority's (ERA) Issues Paper: Annual report to the Minister for Energy on the Effectiveness of the Wholesale Electricity Market (2019 ISSUES PAPER)

Kleenheat has a strong presence in the WA energy market, having retailed LPG to customers for over 60 years and natural gas to residential and commercial customers since 2013 when it introduced competition into a monopoly market. Kleenheat has also sold electricity to commercial customers since 2007.

Kleenheat currently has no wholesale electricity production/generation assets of its own. It operates as a pure retailer and purchases its electricity needs through the wholesale electricity market ("WEM") or via bilateral agreements with Synergy. Kleenheat's experience in operating in the WEM is that it is generally difficult to access wholesale electricity on competitive terms.

We have outlined our responses to the Issue paper's questions in the attached. Should you require any additional detail, or wish to discuss our submission further, please feel free to contact us.

Regards



Nick Rea

Manager, LNG and Wholesale

The remainder of Kleenheat's submission focuses on the issues raised by ERA. Some of these aspects were also identified in previous submissions.

Question (a)

a) Do you agree with the ERA's assessment of how the market is or is not meeting its objectives? Please explain your perspective using examples.

Kleenheat agrees with the ERA and believes the structure and design of the market are not fit for purpose and do not allow the market to fully meet its objectives.

Lack of competition in the South West Interconnected System ("SWIS") as demonstrated by the level of the HHI index of this market impedes meeting the objectives of:

- promoting economic efficiency,
- minimising the long-term cost of electricity supplied to customers in the SWIS, and
- does not encourage measures to manage the amount of electricity used.

For example, the lack of liquidity and term of Synergy Standard Products reduces pure retailers ability to compete effectively with vertically integrated market participants. Electricity customers typically seek fixed pricing for their electricity supply for terms of two to three years or longer. Such tenures are not offered by Synergy under the standard product regime. As such, non-vertically integrated electricity retailers are unable to hedge their offers to end customers to compete in this space. Where products are available, Synergy's allowable bid-offer spread sets a benchmark reference in the wholesale market for bilateral contracting allowing gentailers to benefit from this margin at the expense of a higher cost paid by the end customer.

Question (b)

b) Are there other factors you think the ERA should consider when assessing whether the market is meeting its objectives? Please explain your perspective using examples.

Electricity sourcing through the WEM (STEM and Balancing markets) is generally accessible and transparent as it is cleared by a central operator, AEMO. However, in the absence of facility bidding for Synergy's generators, it is unclear whether there is sufficient pricing discipline on generators (85 per cent of which are owned or controlled by Synergy).

Kleenheat relies on Synergy to source its electricity hedging needs as would many other retailers. Kleenheat typically sources electricity through a combination of back-to-back contracts with Synergy on an ad-hoc basis and fixed blocks of electricity offered as standard products. The Short Term Energy Market ("STEM") and balancing markets offer only marginal portfolio balancing solutions and no hedging solutions. Back-to-back contracts and standard products provide an opportunity for Kleenheat to minimise its price risk exposure under its retailing activity; however Kleenheat's experience in sourcing electricity is that it is difficult to obtain it on a competitive commercial basis. Synergy's back to back and standard products are typically not a viable option for sourcing wholesale electricity, as evidenced by the lack of liquidity in them. This situation ultimately affects Kleenheat's ability to compete effectively in the retail electricity market, where customers expect fixed pricing rather than exposure to a volatile market price. Efficient forward markets will be increasingly important in the future as renewable energy

penetrates the WEM. It will become difficult for market participants to be fully integrated and the need to trade forward products will increase.

In previous submissions, Kleenheat supported the idea of promoting a more liquid wholesale forward market through the use of a mandatory auction process for a quantity of electricity from Synergy, in lieu of the current standard products regime.

Alternatively, some other options include:

- Reducing the bid-ask spread on Synergy standard products to improve the liquidity of both buy and sell products and enforce more price discipline.
- Requiring additional maturities within the current Standard Product regime to allow non-gentailers to hedge longer dated retail offers.
- Transparency of, or assurance that processes for and transfer pricing between Synergy Wholesale Business Unit and Retail Business Unit are similar to that available to competitors as specified under Part 3 of the EGRC regulations 2013 and Synergy's wholesale supply policy.

Question (c)

c) Is the objective of minimising costs to consumers materially compromised by a lack of whole-of-system coordination? What is the best way to ensure that such decisions are in the long-term interests of consumers and meet the market objectives?

Kleenheat agrees that whole-of-system coordination is appropriate to minimise costs to customers and ensure their long-term interest. Power markets are complex structures that require coherent coordination between production, transfer and end use of electricity.

Kleenheat believes current system planning carries some weaknesses. In particular, the relationship between the grid and wholesale markets focuses on optimising either the grid or the market when a new project, rule, or investment is assessed. This can lead to sub-optimal decisions and additional costs to the customer at a later stage. Clarity and transparency about initiatives on the distribution grid and their impact on the WEM are also required.

Furthermore, the alignment of Western Power Access Arrangements with AEMO planning would optimise and facilitate third party investment decisions and deliver value in the long-term.

Finally, government initiatives and incentive plans are not assessed on their impact on the entire grid and should be linked to a whole-of-system plan to avoid an overall increase of cost to the system.

Kleenheat recommends the following changes:

- Independent body to gather and assess the holistic value of any initiative. The ERA is ideally positioned to fulfil this role.
- Alignment of planning timelines (Access Arrangements, ancillary service requirements and Electricity Statement Of Opportunities).
- Transparency of initiatives, funds, accesses and subsidy mechanisms.
- Simplification of committees and decision-making forums.

Question (d)

- d) Do stakeholders share the ERA's concerns about rule changes to enable market development post reform? Should a single entity be given responsibility for ongoing market development? If so, which entity is best placed to have this responsibility and why? What governance arrangements should be placed on that entity?*

Affordable electricity should be a key focus, particularly post-reform. ERA would be the appropriate single entity to ensure such an outcome, and Kleenheat is supportive of an independent authority responsible for the entire system.

An arrangement similar to the Market Advisory Committee ("the MAC") would be appropriate; however, greater representation of market customers would ensure affordability is not compromised, based on ERA cost-benefit analysis from a holistic system perspective. This would help deliver long-term market solutions with the least cost outcome for customers.

Under the current MAC structure, entities impacted by the outcome may undertake technical or economic analysis, which at times may impact an optimal decision being made in a timely manner. Independent cost-benefit analysis by ERA would overcome this issue and focus on delivering optimal long-term market solutions to meet WEM objectives.

Question (e)

- a) Do stakeholders share the ERA's concerns about the rule change process? How could the rule change process be changed to ensure parties progress rule change proposals in line with priorities prescribed by the MAC and the Rule Change Panel?*

Kleenheat shares the ERA's concerns about the current rule change process. Post-reform, the MAC requires greater representation of market customers and an independent entity (e.g. ERA) providing analytical updates to the MAC (ie: AEMO, Western Power and market generators should provide data / information for ERA analysis) to ensure the least-cost / optimal outcomes for the market via a single, impartial entity.

Cost-benefit analysis by an independent entity would drive faster rule-change related decision-making, reduce meetings and committees, and deliver more timely solutions to complex issues.