



Premier Coal

Wesfarmers Premier Coal Limited ABN 21 008 672 599
Premier Road, Collie, WA, 6225
Postal Address: PO Box 21, Collie, WA, 6225
Telephone: (08) 9780 2222, Facsimile: (08) 9780 2223

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Discussion Paper: Annual WEM Report to the Minister
Economic Regulation Authority
PO Box 8469
Perth Business Centre
PERTH WA 6849

E-Mail: SubmissionMinReport@era.wa.gov.au

Dear Sir,

Discussion Paper: Annual WEM Report to the Minister

Wesfarmers Premier Coal ("Premier") is pleased to take this opportunity to respond to the above discussion paper. As a major supplier of coal to Verve Energy ("Verve"), Premier has a keen interest in the effectiveness of the Wholesale Electricity Market (a separate submission will be made by our retail company, Wesfarmers Premier Power Sales).

In considering this response, Premier has particularly focused on the following wholesale market objectives (Premier's underlining).

- To promote the economically efficient, safe and reliable production and supply of electricity and related services in the South West Interconnected System ("SWIS").
- To minimise the long-term cost of electricity supplied to customers from the SWIS.

Premier has supported electricity reform in Western Australia on the basis of the above objectives and a critical element in this support is a level playing field for primary energy suppliers, electricity generators and retailers. It was on this basis that Premier and Verve Energy negotiated a long-term 'all requirements' contract for the supply of coal to the Muja, Collie and Kwinana power stations.

The comments below reflect our desire to ensure that policy consistency is maintained in the operation of the electricity market in accordance with the market objectives. We accept that various arrangements were put in place to ensure that new market participants were encouraged, such as Verve's 3,000MW cap, however we believe that the some aspects of the market's operation have imposed unfair cost and operational imposts on Verve that are inconsistent with the market objectives.

Discussion Point 1

“Given the current Wholesale Electricity Market design, the authority invites comments on the extent to which the operation of the Reserve Capacity Mechanism is effective in achieving the objects of the Wholesale Electricity Market.”

Premier views with some concern the outcome of the capacity credits assigned for the Third Reserve Capacity Credits Cycle (1 October 2009 to 1 October 2010). This process assigned 5136 MW of capacity credits, compared with a forecast requirement of 4609 MW (an excess of 527 MW). According to the Independent Market Operator Statement of Opportunities Report, the total reserve capacity target does not reach 5136 MW until 2013/14. The capacity mechanism has delivered a significant level of excess capacity (with a high proportion of peaking units) that may distort the market and its operation and provide inappropriate investment signals for the next few years.

The market objectives clearly call for a non-discriminatory approach to all energy options. It is apparent that the current capacity mechanism positively discriminates in favour of wind energy, as it must be dispatched when it is available, and there is no penalty for any variation from planned availability. Wind is the only energy source to receive this dispensation.

Furthermore, we understand that Verve is compelled to absorb wind power when it is available and reduce its generation by other units. As wind power is often available overnight, Verve has to bear the cost of shutting down efficient baseload power stations to accommodate unpredictable wind generation by third parties. Other generators are not required to reduce generation to accommodate wind power, leaving Verve in a disadvantaged position in the market.

Discussion Point 2

“Bearing in mind the interaction of the capacity market and the energy market, the Authority invites comment on whether the current Wholesale Electricity Market provides adequate incentives for an efficient mix of generation plant.”

From our regular interaction with Verve Energy, in relation to coal supply matters, it is apparent that Verve’s base load plant is increasingly operating as mid merit plant. We view this as an inefficient outcome that potentially increases the cost of electricity, given that the efficient baseload coal-fired plants at Muja and Collie incur additional costs and face technical issues when operating in a mid merit configuration. The operation of wind energy, as noted above, also contributes to this inefficient outcome by displacing Verve’s efficient base load plant.

Discussion Point 3

“The Authority invites comment on any fuel supply constraints faced by market participants and the impact any such constraints have on the effectiveness of the Wholesale Electricity Market. In particular what impact, if any, do fuel supply constraints have on the operation of markets for capacity and energy?”

The discussion notes on this point suggest that some market participants consider that gas supply problems impact on the Wholesale Electricity Market. Although we are not in a position to comment on any gas pipeline issues, Premier's strong view is that gas supply and pricing should be considered in the context of a broad state energy market.

Some parties contend that government intervention in the gas market is necessary to ensure supply. We believe that previous government intervention caused a hangover of artificially low gas prices that may have led to false expectations of what constitutes fair gas prices today. Indeed, these artificially low gas prices have encouraged investment in liquefied natural gas for export markets at the expense of domestic supply.

We have already seen evidence of the market impact of increased gas prices, with the recent announcement by Apache Energy of a new gas project, which will be supplying gas to the domestic market.

The operation of market pricing signals and "gas on coal" competition will ensure the most competitive long run fuel availability and costs for market participants. The Western Australian energy supply market must be allowed to operate without government intervention; this will lead to the most economically efficient outcome in accordance with electricity market objectives.

We thank you for the opportunity to provide comment on this discussion paper and look forward to the outcomes of the consultation process.

Yours sincerely,
Wesfarmers Premier Coal Limited

W. J. Moody
General Manager, Marketing and Development

Respond to:

W. J. Moody
General Manager, Marketing and Development
Wesfarmers Premier Coal Limited
PO Box X2231
PERTH WA 847