

INTRODUCTION

The Energy Users' Association of Australia (EUAA) is the peak body representing Australian commercial and industrial energy users. Our membership covers a broad cross section of the Australian economy including significant retail, manufacturing, building materials and food processing industries. Combined our members employ over 1 million Australians, pay billions in energy bills every year and in many cases are exposed to the fluctuations and challenges of international trade.

As large energy users, our members are highly exposed to movements in both gas and electricity prices and have been under increasing financial stress due to escalating energy costs. These increased costs are either absorbed by the business, making it more difficult to maintain existing levels of employment or passed through to consumers in the form of increases in the prices paid for many everyday items.

We welcome the opportunity to make a submission to the Capacity Mechanism High-Level Design Paper (Design Paper). We have already made a submission to Project Initiation Paper (February 2022) and are pleased to see that a number of issues we raised have been reflected in the Design Paper, although much more work needs to be done on detailed design and cost benefit analysis before consumers can be sure that a capacity market will deliver promised benefits.

Based on member feedback and our own experience to date, the true nature of the problem we are trying to solve has not been made abundantly clear. That is not to say some form of capacity market is not required (we expand on this later) but more specifically what is the duration of capacity gap that we are concerned will not be met with existing market settings. This Design Paper starts to answer some, but not all of these questions.

The current EUAA view is that short duration capacity, or intra-day capacity gaps (i.e. up to 4 hrs), may well be met with existing (FCAS) and emerging (ESS) market settings (along-side energy market revenue) and that a capacity payment would simply represent an over-payment to those technologies. Our current view therefore is that the true problem is the longer duration (6+ hrs), or inter-day capacity gaps that may continue to emerge.

We are keeping an open mind to issues associated with both intra-day and inter-day capacity gaps and to getting a more complete understanding of the nature of the problem and if a solution, such as capacity payments, will deliver material benefits to consumers or simply line the pockets of market participants.

NATIONAL ELECTRICITY OBJECTIVE

As always, we remind all stakeholders of the National Electricity Objective (NEO) being.

"to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers¹ of electricity with respect to: price, quality, safety and reliability and security of supply of electricity.

¹ *Emphasis Added*

Too often consumers see policy being proposed that is in the interests of others including investors, market participants, technology providers, developers, shareholders or even governments. While we should pursue opportunities where interests are aligned, the long-term interests of consumers should never be subservient to the interest of others.

Therefore, we are pleased to see that achieving outcomes consistent with NEO are explicitly spelled out for stakeholders on page 4 of the Design Paper. We see a range of other design principles identified by ministers on page 5 of the Design Paper (box 1), most of which are consistent with achieving the NEO with the exception of:

“jurisdictions must be able to determine, via their regulation, provided for in the National Electricity Law framework, which technologies are eligible for participation in a capacity mechanism in their region”

and

“recognise relevant state and territory policies and investment schemes to account for bespoke arrangements to retain and replace existing capacity”

and

“enable jurisdictions to opt out, via the national Electricity Law framework”

We understand the ESB are taking a pragmatic approach to policy design, recognising that state jurisdictions are likely to derogate away from a national approach should they perceive that it is not aligned with their political interests or policy goals. However, given we believe that the NEO is best achieved via a nationally consistent approach to energy policy, we do not see how the highlighted design principles will contribute to the long-term interests of consumers.

A guiding principle for all energy policy and regulatory design is to achieve net zero at least cost, not at any cost. Therefore, design criteria that seeks to minimise total consumer costs must be at the forefront of design of any future market or policy. The absence of consumer costs as a consideration makes it difficult for a potential capacity mechanism (or any policy or regulation) to meet the NEO.

THE CASE FOR CHANGE

As we have said in previous submissions, the energy transition is resulting in the accelerated exit of traditional dispatchable fossil fuelled generators that to date have provided energy users where a bundle of services that were folded into the provision of energy including dispatchability, system strength and inertia. While the provision of zero emission energy is of great value, Variable Renewable Energy (VRE) alone is not currently required (or able) to provide a number services vital to the reliable operation of the energy system. From an energy system perspective, 1MWh of energy from VRE is less valuable than 1MWh of energy from traditional sources.

The unbundling of these services, including capacity/dispatchability means they now need to be provided (and priced) separately. In recent years we have begun to see the costs of this unbundling become more material with the increased frequency and cost of AEMO market interventions (RERT, Market Directions etc) and increasing FCAS cost, although it must be said that some of these costs are a result of other factors such as generator bidding and escalating gas costs making gas peaking plant uneconomic at times. Some members have also expressed concern that some of these costs are being influenced by supply side market power issues, the management of which needs to continue.

A combination of a number of issues, including those listed above, contributed to the recent unprecedented market suspension by AEMO. In reality the issues that led to this market suspension have been bubbling up for a number of years with both the causes and solutions subject to furious debate.

While the causes behind the market suspension, such as fuel availability, are being fully investigated we should treat the last few months as a painful and expensive learning moment. It has given us a glimpse of a potential future where the transition to net zero has not been well managed due to a lack of broad based, pragmatic, technology neutral approach to policy that focuses on the NEO.

While many questions remain, we are in broad agreement of the scope of the proposed capacity mechanism being:

Ensuring investment in an efficient mix of variable and firm capacity that meets reliability at the lost cost by:

- *Facilitating the timely entry and exit of new generation, storage and flexible resources*
- *Facilitating or complimenting the orderly retirement of ageing thermal generation*
- *Complementing other market arrangements addressing resource adequacy*

The coordination of the exit and entry of appropriate resources in the most efficient manner is of critical importance to the long-term interests of consumers. We must move away from the current ad-hoc, highly disjointed, multi-jurisdictional approach as this approach does not satisfy the NEO.

In particular we must:

- Be wary of an approach that simply calls for more VRE technology to be deployed in the hope that it will somehow fix the issues created by increasing levels of VRE technology.
- Reject an approach of “the sun will be shining and the wind will be blowing somewhere so if we build enough VRE we can plug the gaps” as this simply leads to an unnecessary and very expensive overbuild of the energy system with no guarantee that long-duration gaps will be filled. Equally, we are not convinced that off-shore wind will provide a materially better capacity outcome than it’s cheaper on-shore cousin as both are weather dependant technology that alone are not capable of being dispatched on demand.
- Challenge an approach where encouraging the deployment of batteries (either via capacity payments or subsidy scheme) with an export duration of 2-6 hours will alone resolve the longer duration gaps in supply and reliability that are emerging. The AEMO 2022 ISP calls for 10GW of gas generation as part of a broad portfolio of technologies (including pumped hydro) to meet the future energy market needs² which highlights the need for a technology neutral approach.
- If gas is to play a key role (we think it should) then governments must act to ensure it is available for domestic use at an affordable price.
- We can’t continue down a path where the exit of thermal generation is managed by a series of secret, back room deals between generators and governments as we have seen with the arrangement between the owners of Yallourn power station and the Victorian Government³ or recent negotiation between the owners of Eraring power station and the NSW Government⁴. If governments are to play this role (which may prove to be the only way), then a far more transparent and economically efficient (i.e. competitive) approach is required.

² <https://aemo.com.au/-/media/files/major-publications/isp/2022/2022-documents/2022-integrated-system-plan-isp.pdf?la=en>

³ <https://www.afr.com/companies/energy/yallourn-deal-further-distorts-power-market-20210315-p57atw>

⁴ <https://www.afr.com/politics/nsw-government-knocked-back-origin-offer-to-sell-eraring-power-plant-20220614-p5atln>

- We must strive for a nationally consistent approach to energy market reform to avoid unnecessary, inefficient investment and duplication of consumer costs.

In our engagement with members on the capacity mechanism, it is becoming clear that less questions remain about the need to do something (this is coupled with a growing view that to do nothing is not in the long-term interest of consumers), but many questions still remain around the ability of a capacity mechanism to achieve the desired outcome at least cost to consumers and without providing market participants, old and new, with windfall gains.

Feedback from member companies includes:

- A strong desire to make a capacity market as least cost as possible; in particular the need to avoid the propensity to reward market participants for doing something they should have done or would have done anyway. This extends to short duration batteries where it appears sufficient signals already exist or are quickly emerging (i.e. expanded FCAS and Essential System Strength requirements). Recent announcements of non-subsidised battery investments tend to support this view⁵
- They question why existing mechanisms such as the Retailer Reliability Obligation have not been given an opportunity to deliver the desired outcomes. They are concerned that it appears governments have lost faith in the market to deliver the desired political reliability they seek so will continue to intervene, even if a capacity market is in place.
- They are adamant that the focus should be on the ability to deliver MWh (actual electrons) not MW capacity (nameplate value is irrelevant) on demand at a time that is required. While they appreciate that the proposal of de-rating of participants and post event compliance will be critical to managing this, they wonder if a more explicit requirement of “capable of dispatch” would be more appropriate.
- They are adamant that the reliability standard should continue to be determined by the independent Reliability Panel and that the current reliability standard of 0.002% of USE should be maintained. The EUAA and its members have never supported the interim reliability standard of 0.0006% of USE due to the additional costs it could generate for limited if any material consumer benefit.

PARTICIPATION OF NEW AND EXISTING CAPACITY

The EUAA has a policy of technology neutrality and therefore we are in favour of a technology neutral approach to capacity market design, recognising that the net zero targets of state and federal governments and many Australian business (including many EUAA members) will remain at the forefront of policy design and corporate decarbonisation strategy.

We do not see an inconsistency between the federal government’s commitment of a 43% emissions reduction by 2030, net zero targets (the emphasis being on net zero) and a technology neutral approach to capacity markets (or appropriate gas market reforms for that matter).

While we agree with the ESB that technology neutrality is appropriate, the inclusion of existing assets is a different question and should be dealt with separately. It also raises a series of substantially harder questions that need to be resolved if consumers are to become comfortable that the proposal satisfies the NEO.

⁵ <https://www.afr.com/companies/energy/big-battery-to-power-2-5b-data-storage-project-20220707-p5azzw>

Like the ESB, we do not see this as a “coal keeper” policy (although it could be if poorly designed) as it has been described by some stakeholders with a vested interest in deploying only new technology (to the direct benefit of their members and their shareholders) at the expense of energy users.

The ESB clearly states on page 18 of the Design Paper

“For the avoidance of doubt, the purpose of a capacity mechanism is not to extend the lifespan of ageing thermal generators. These generators face several structural challenges as the NEM transitions to a VRE based system.”

We see this as a potential opportunity to design a mechanism that facilitates the orderly exit of ageing thermal plant so as to avoid a continual repeat of the secret negotiations we have already witnessed. For consumers to fully support that which is proposed in the Design Paper, we would need to see a capacity market that facilitates the orderly exit of ageing assets that doesn’t result in windfall gains for generators, that contributes to maintaining the 0.002 reliability standard and facilitates the entry of new technology capable of delivering services the market requires.

We are not sure all of these objectives can be achieved with a single mechanism but will keep an open mind to the possibility. One thing we are sure of is that chaotic exit of the old and disorderly entry of the new is not in the interest of consumers.

As we engage with member companies and other stakeholders a number of issues have emerged that would need to be resolved for the inclusion of existing assets to be fully endorsed.

In particular, the inclusion of existing assets in the capacity mechanism has raised significant issues amongst member companies with some questioning if a capacity mechanism is the most appropriate vehicle to manage generator exit at least cost.

By including them in the capacity mechanism, it could be argued that squeezing the most from existing resources could lead to an economically efficient outcome as it could avoid the costs associated with bringing forward new capacity long before it was needed.

We observe the theory as articulated by ESB on page 17 of the Design Paper:

“The ESB considers whole-of-market mechanism beneficial because it enables all capacity options to be assessed and the lowest cost options procured. A mechanism that only supports new capacity has only one lever to address a forecast reliability gap – supporting investment in new capacity. In some cases, paying to retain existing capacity may be more efficient than incentivising a new entrant into the market following an exit.”

However, this economic benefit (the extent of which is yet to be quantified) needs to be weighed against the potential of windfall gains being gifted to assets that already have a sunk cost, that are already underwritten to a degree by long-term sales agreements or have already received significant government support (grants, government contracts or CFD style incentives such as those proposed in the NSW energy infrastructure roadmap).

These concerns are amplified by the deteriorating reliability of ageing thermal plant and the escalating costs to keep them running. If the costs of running these ageing thermal plant (with the proxy being the value of capacity payments required) is greater than the economic efficiency benefits of keeping them going (and the risk of windfall gains) then the value of including these existing assets is doubtful. This equation may be different from generator to generator depending on age, condition, fuel source etc. We believe that “solving” this equation is critical to an outcome that is consistent with the NEO.

It could be that a competitive capacity auction process with a price cap set at an economically efficient level (economically efficient for consumers, not generators) could resolve this. In any case, energy consumers would need to clearly see how a capacity mechanism would assist these assets without consumers incurring significant costs as they underwrite the increasing op-ex spend. In the absence of detailed economic analysis of this trade-off, it is impossible to reach an informed view.

Some members have expressed a view that given the declining reliability of ageing thermal plant and the risks associated with failure to deliver, it is not unreasonable to think that many existing generators would either not participate or would need to put in place a back-to-back contracting structure to mitigate this risk, with the former the most likely scenario. If this is the case, ageing thermal assets may not have the level of participation that some have feared. If so, then the ability of the capacity mechanism to manage the exit of ageing thermal plant, and therefore play a role in the security of the system while new assets are deployed, is significantly reduced.

Depending on this outcome, perhaps alternative approaches to the orderly exit of ageing thermal plant needs to be considered. For example, while we have been critical of secret government negotiations with generators, the key issue is the lack of transparency and competitive tension. If an orderly exit strategy was underpinned by a transparent auction process where governments manage a form of closure contract that is on the jurisdictional balance sheet, where consumers and markets have clarity about timing of closure and cost, then it may prove to be a worthwhile approach. This could also avoid issues associated with lowering the MPC (which we support) and economic neutrality of those generators who may be excluded from the capacity market but no longer have access to a high MPC. This “out of market” capacity mechanism, including capacity auctions is similar in principle to that proposed in this Design Paper but it is government that takes the risk on behalf of taxpayers, not energy users.

We would emphasise that there is no perfect approach to orderly exit so in the absence of perfection an approach that provides the maximum amount of transparency, accountability, stability and energy consumer protection should be pursued.

It is not just the circumstances surrounding existing thermal assets that need to be carefully studied. There will be existing assets that have been installed recently (i.e. batteries) that have already received significant public support via government grants and contracts. For example, the emerging Storage LTESA’s being developed by the NSW government will see 2GW of storage underwritten by NSW energy users⁶. We would argue that as these assets are already being underwritten by energy users and taxpayers, their participation (or not) needs to be carefully considered. If they are to participate, should they be required to return grant funding or exit from existing contacts with government? Could a form of de-rating be applied based on incentives already received? These are significant design questions that consumers would need answered in forthcoming engagement.

⁶ <https://www.energy.nsw.gov.au/sites/default/files/2021-08/long-term-energy-services-agreement-design-consultation-paper-210316.pdf>

Regardless of technology type, to ensure consumers receive value for money, a principle of additionality should be considered when assessing eligibility. For example, some members have suggested that capacity payments should only be made where it is clear that additional capacity is being provided as a result of the capacity payment and we are not simply providing additional revenue for BAU activities.

The need to re-consider the Market Price Cap (MPC) should a capacity market be introduced is a strong theme amongst energy users. A high MPC is designed to send a price signal for new investment. If a capacity market is designed to fulfil this role (providing a large part of the investment signal) then a lower MPC should follow. We are of the view that maintaining a high MPC along-side a capacity market has the real potential to deliver windfall gains to all generators.

We recognise that lowering the MPC may create issues for existing assets who are excluded from the capacity mechanism as they would no longer be able to access a higher wholesale price that was relied upon to underpin their initial investment. One solution could be to consider a split MPC, where those taking capacity payments access a lower MPC, while those who do not receive capacity payments access a higher MPC.

Market power continues to be a topic of concern for energy users. Extreme care must be taken when designing any new policy that market power is not “gifted” to one group of participants. This is a particularly acute issue where existing assets are eligible to participate in the capacity mechanism or if the capacity mechanism design allows participants to “game” their position to receive additional benefit.

Finally, a number of questions have been raised relating to how existing long-term contracts (i.e. PPA's) will be impacted by these changes and the need for grandfathering provisions to protect customers from unintended consequences and unexpected cost pass through under change of law provisions.

DEMAND SIDE PARTICIPATION

We are strongly in favour of encouraging demand side participation in a future capacity mechanism. However, we would point to issues encountered by large energy users as they sought to engage on the Wholesale Demand Response Market (WDRM) design. Large energy users found the obligations that would be placed on them created a significant barrier to entry. This led to the establishment of the scheduled lite approach as a first step to encourage large energy users to begin participating in demand response without the threat of penalty.

Given our experience so far, demand response (and potentially capacity market participation) is more likely to appeal to aggregators and existing market participants such as retailers who take on market risk and share benefits with participating customers. Further, large energy users are attracted to RERT participation given the voluntary, lower risk nature of the scheme. It is unclear how the barriers to participation already encountered with the WDRM will be resolved by capacity market design.

Similarly, the interaction between the capacity mechanism and existing mechanisms that seek to use the same resource (WDRM and RERT) is also unclear.

A number of members have made point that as large industrial loads entering into a long-term contract for the delivery of energy, they are already underwriting/paying for capacity. A capacity market (charge passed through by AEMO) would effectively see them pay twice for capacity they have already procured.

There is a firm view that large energy users who have entered into long-term, fixed volume contracts:

- Are already underwriting a level of system capacity and stability
- Are reducing the volume of capacity that AEMO will need to procure
- Are reducing the cost burden for all consumers
- Should not have to pay for capacity twice

Therefore, we suggest that:

- AEMO includes these long-term, fixed volume contracts when assessing capacity needs so as to avoid over-procurement of capacity (and therefore reduce the overall cost burden)
- Reduces the capacity costs for these large energy users who enter in long-term, fixed volume contracts

For example, if a large energy user enters into a long-term (i.e. 5 years), fixed volume contract (i.e. for 75% of their total load) then they should only be liable to pay 25% of the capacity costs. The higher the fixed volume the lower the liability. This would avoid them paying twice for capacity plus it would encourage more large energy users to enter into these contracts, and in doing so reduce the capacity market costs for all energy users.

This is not an exemption from the scheme but a recognition of the important role that large loads already play in maintaining capacity and system security. We feel that the key role played by large industrial loads is not well understood or recognised. We were surprised with the ESB view, expressed on page (i) of the Design Paper, that questioned the longevity of major energy users such as smelters.

We can only reiterate the importance of large loads such as smelters, all of whom have existing long term contracts. We understand from the Australian Aluminium Council that the expiry of these contracts varies from 2025 to 2029, that the owners of Australia's four smelters have not given any indication of intentions for these loads to exit and have signalled their desire recontract renewable electricity at the end of the current terms⁷

FORECASTING CAPACITY

As we have stated in our previous submission to The Project Initiation Paper we are initially drawn to a decentralised, market based approach to forecasting and procurement. This approach would be more akin to the Retailer Reliability Obligation. Members believe that a decentralised approach would be more likely to empower the consumer to make decisions most appropriate to their needs. For example, many large industrial loads use multiple strategies to "firm" their energy needs including:

- Buying fixed price volume variable agreements (the traditional retail arrangement), where they transfer risk in return for an embedded shape risk premium
- Buying swaption type arrangements with spot exposure but using curtailment to effectively reduce load in times of market stress
- Shaping PPAs to be "firm" as opposed to run of plant, transferring shape risk to someone better suited to manage for a premium

⁷ <https://www.riotinto.com/news/releases/2022/Rio-Tinto-calls-for-proposals-for-large-scale-wind-and-solar-power-in-Queensland>, <https://www.afr.com/companies/energy/4b-offshore-wind-farm-proposed-to-power-smelter-20211207-p59fe4>

- Investing in multiple types of embedded generation: batteries, combined heat and power, solar PV to offset peak and baseload demand
- Optimising heat vs power outcomes to reduce exposure (with the effect of lowering our grid demand)
- Investing in power stations generation development
- Investing in demand flexibility in order to be able to respond to electricity market price signals

Through these actions, large loads are already supporting market capacity, as we have already discussed. The extent to which future market design facilitates or hopefully enhances industrial loads to continue this innovation will be an important consideration.

Having said that, it is clear that a decentralised approach does not appear to deliver the level of confidence required by governments so the ESB have moved in a different direction.

A highly centralised approach, while not supported by the EUAA, seems to provide the level of certainty governments are seeking. We appreciate the ESB recognising consumer concerns on page 22 of the Design Paper where it states:

“However, several stakeholders have raised concerns that a central body (such as AEMO as system operator, with responsibility for system reliability), may take a conservative approach to forecasting capacity requirements. Stakeholders argued that while this may increase confidence for governments that reliability gaps will be addresses, it could lead to increased costs for consumers if it results in over procurement.”

How do we avoid this over-procurement (or at least reduce the likelihood or quantum)? We would offer the following:

- Potentially expand the role of the reliability panel to provide advice on the link between a consumer led reliability standard that takes into consideration the intersection of costs, willingness to pay and reliability.
- The AEMO ISP Consumer Panel has been a very good initiative which we believe has contributed to a significant improvement in the 2022 ISP and joint understanding and trust between consumers and AEMO. Consideration should be given to establishing a similar group (i.e. Capacity Market Consumer Panel) to provide a level of independent oversight and advice.
- Ensure transparency of forecasting methodology and approach. Large industrial loads and retailers could play an enhanced role in this process given the joint objective of minimising costs and risk.

In our response to the Project Initiation Paper in February 2022 we identified a number of design principles that we felt were missing including:

- Clear definition of capacity: A clear definition of capacity will determine the applicability of a capacity mechanism for different industries (i.e. what capacity is needed for what purpose). As the ESB resolves this definition, the key issue will be ensuring that only truly dispatchable entities (including load) are eligible to receive payment and ensure compliance processes support this.
- Capable of dispatch: If an asset is to receive a capacity payment it must be capable of dispatching that capacity (or a specific part thereof) on demand.

While de-rating of capacity may deliver a similar outcome to capable of dispatch we feel that a stronger definition of capacity is required. If governments are seeking greater comfort that the capacity mechanism will mitigate political risk, then surely a stronger definition of capacity is required that does not overly rely on anticipated outcomes of a de-rating process. A capable of dispatch definition may also add clarity and simplify determinations of “At-Risk Periods” and “Compliance Periods”.

We are in general agreement of an approach that seeks to identify the periods most likely to suffer from a capacity gap and to ensure resources are available to fill that gap when required. At this point in time we are not in a position to assess the merits of the options proposed in the Design Paper so look forward to more detailed analysis being presented as we engage further.

Regardless of the methodology, these more targeted approaches, while still likely to deliver an imperfect outcome due to forecasting errors etc, does lend itself to a more efficient allocation of the right resources to do the job (i.e. short duration v long duration) and may help to alleviate some over procurement fears that consumers have.

A more targeted and thoughtful approach is certainly preferable to a simple but arbitrary subsidy scheme for batteries that rewards installation of technology (at consumer cost) but not the capacity or reliability outcome we require. Simply dotting more short duration batteries around the country won't solve the complex problems faced by the NEM and would not have been much help dealing with the situation leading up to and during the recent market suspension, which was primarily a long-duration problem.

PROCURING CAPACITY

We re-iterate our preference for a decentralised procurement approach, however we recognise this may not provide governments with the level of comfort they require. If centralised procurement is pursued then a competitive auction approach seems appropriate and assuming a level of transparency is provided, ensure to a degree that market participants are able to make rational financial decision.

Transparency is also important for consumers who often suffer from information asymmetry where the seller is able to extract additional value from customers who are unable to verify or reject the basis of the cost pass through. Assuming a high level of transparency and competitive tension is achieved, the procurement approach is less important than the forecasting approach, eligibility criteria and compliance. Forecasting will set the level of demand, eligibility will dictate the participants/suppliers and compliance will ensure the insurance policy consumers are purchasing is there when we need it.

The focus of procurement must be on ensuring transparency and maximising competition amongst participants. It would also be helpful to consumers if capacity certificates had a ceiling price or cap over which it is deemed uneconomic or inefficient for consumers to pay. Everything has a limit and consumers should not be asked to underwrite capacity at any cost, just like we should not be pursuing net zero at any cost, but at least cost.

OBLIGATIONS OF CAPACITY PROVIDERS

Our views are very much driven by the principle of capable of dispatch as it removes some of the doubt around de-rating and post event analysis of performance.

To be very clear, we believe that capacity payments represent a contract between the customer and capacity provider. A breach of that contract by the capacity provider should not be treated as a minor infringement but a failure to meet their contracted obligation.

Therefore, our views on the obligation of capacity providers are simple:

- If we pay you for capacity you must deliver when required
- If you do not deliver when required you must hand back all capacity payments made for the period that you had committed to
- If you do not deliver when required you should also face the prospect of civil penalties
- If you do not deliver on a number of occasions you will be expelled from the capacity mechanism (i.e. 3 strikes and you're out)

TRANSMISSION

Considering how transmission can facilitate more efficient sharing of capacity resources is important. The EUAA are becoming increasingly concerned with a jurisdictional approach to energy policy leading to a balkanisation of the NEM, inefficient resource allocation, duplication of effort and unnecessary costs being incurred by energy consumers.

Quite clearly if regulated transmission where to participate in a way that allowed them to gain financial benefit (either via additional revenue or the capacity transfer benefit was used as part of RIT-T assessment), then any financial benefit received must reduce the amount of TUOS that consumers pay.

Including the capacity transfer role that transmission could play allows capacity in one jurisdiction to benefit consumers in another jurisdiction, resulting in an efficient sharing of resources. Therefore, even if a jurisdiction refuses to allow participation by a certain technology or asset in their jurisdiction it does not preclude that technology or asset participating in the capacity market in another jurisdiction. To prohibit that technology or asset from using private transmission assets to sell a product into a jurisdiction that allows its participation could potentially be deemed as restraint of trade. It will be interesting to watch this situation unfold over the coming months.

OTHER ISSUES

We have not formed strong views on other aspects of the Design Paper but member companies offer the following for consideration:

- Cost allocation via retailers seems the most logical approach given they already have systems in place to facilitate this.
- A design element that should be considered is that capacity market costs should be capable of being passed through as a fixed cost to large electricity consumers. This necessitates that the design of the capacity market provides a liquid contracting market that trades years ahead to allow retailers to hedge their exposure and provide fixed pricing when quoting electricity consumers.

- The capacity market should be defined to avoid any double dipping by generators. We need to avoid the instances where generators seek to maximise profit at the expense of consumer by generating additional revenue but not providing an additional service.
- In developing a capacity market that sits alongside the energy only market consumers will be focussed on the total cost of the reform, not just the impact of individual pieces. It is the impact on the final bill that is important for energy users and we ask that the ESB is similarly focussed on this outcome.

TRANSITIONAL ISSUES

As we have already stated, most large commercial and industrial facilities have long term electricity contracts in place that contain a range of change-in-law provisions meaning energy users are not immune to changes in the market. Many EUAA member companies feel that existing long-term contracts (including VRE PPA's) need to be grandfathered in some way, especially where such a significant change in the market structure is being proposed.

Some member companies have identified the potential impact on VRE PPA structures:

- A typical run of plant deal becomes extremely risky (where generation output is variable and may not match counter party consumption), particularly for load who have some demand elasticity
- Firmed offtake agreements i.e. such as those designed to match an ASX Swap products under PRS framework, which technically have a firmness factor of 1 become invalidated
- Potential for double pass through from the asset owner (on the generator side) and retailer on the pool passthrough on capacity
- ASX products become somewhat invalid based on design choices - i.e. Swap becomes more complex given the makeup of capacity + energy only + cap

Once again, thank you for the opportunity to make this submission. Do not hesitate to be in contact should you have any questions. We look forward to engaging with the ESB over the coming months.

Kind regards,



Andrew Richards
Chief Executive Officer