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Mr John Pierce AO
Chair
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Dear Mr Pierce

Submission to Draft Determination on Transmission Loss Factors rule change

Thank you for the opportunity to comment on the Australian Energy Market Commission's (AEMC) draft rule determination for the Transmission Loss Factors rule change process.

We support the AEMC's draft decision to:

- retain the existing marginal loss factor (MLF) methodology, rather than moving to an average loss factor methodology, and
- retain the allocation of intra-regional settlement residue (IRSR) entirely to transmission network service providers (TNSPs) to offset transmission use of service (TUOS) charges paid by consumers, rather than sharing the IRSR with generators.

Background

Changes in MLFs reflect changes in actual physical electrical losses in the transmission system as new generation connects. As the AEMC and other stakeholders have accurately highlighted, the recent volatility of MLFs is a result of the current transition of the NEM's generation profile:

- The NEM is forecasted to replace most of its current generation stock by 2040.¹
- The profile of new generation connecting in the NEM is moving towards a larger number of relatively small and geographically dispersed generators.
- These generators are connecting in remote areas of the network to locate near fuel sources (e.g. where it is windy or sunny), which lack transmission capacity or which are a significant distance from load (in turn, contributing to high losses).

¹ AEMO, Integrated System Plan (July 2018), section 3.1.2, p. 33. Available at: https://www.aemo.com.au/-/media/Files/Electricity/NEM/Planning_and_Forecasting/ISP/2018/Integrated-System-Plan-2018_final.pdf

- New generation is able to connect at a relatively rapid rate due to the speed of construction with which new generation assets can be built. This means that changes to MLFs occur more frequently as the result of new generation rapidly connecting to the network.
- The new generation plants often have correlated, rather than offsetting, dispatch characteristics, which can contribute to congestion and, in turn, losses.

It is important to provide investors with clear market signals as to the areas of the transmission network that have capacity or are close to load. The efficient siting of generation in the network will help to minimise losses and improve the efficiency of transmission investment, ultimately reducing electricity costs for consumers.

These signals, alongside other factors such as the availability of fuel sources, should inform investors' decisions of where to locate new generation projects. The AEMC's recent Transparency of New Projects rule change, which provides the market with improved information about potential new generation projects, and the Australian Energy Market Operator's (AEMO) quarterly publication of MLF estimates will also aid these decisions.

The AEMC's current Coordination of Generation and Transmission Investment (CoGaTI) review is also considering how best to improve locational signals for investors in new generation.

The proposed rule changes

The AEMC's analysis demonstrates that Adani Renewables' rule change proposals, if adopted, are expected to result in an overall increase of costs and risk to consumers. This includes:

- increased Transmission Use of System (TUOS) charges to consumers as a result of both lower IRSR contributions and greater risk of negative IRSRs, and
- the potential for generators to be dispatched in a less efficient merit order.

Further, any reduction in the cost of capital arising from the adoption of more stable average loss factors would be at the detriment of consumers. Under an average loss factor methodology, consumers would be taking on some of the risk of poor generation investment decisions, which they cannot respond to or manage.

We support the AEMC's draft decision that the rule changes, as proposed, would not be in the long term interests of consumers nor better achieve the National Electricity Objective (NEO). We also agree that, as consumers bear the full costs and risks of the shared transmission network, it is appropriate that IRSR be fully allocated to customers to reduce these costs.

Addressing the cause of loss factor volatility

The recent volatility of MLFs is a result of the electricity sector's current transition. We agree with the AEMC's view that the adoption of average loss factors would be a move away from the long-term direction of reforms in this area. Dampening the locational signals provided by the current MLF approach will give way to new generators connecting to parts of the transmission network with high losses, in turn increasing the volatility of loss factors, as well as increasing costs to consumers over the long term.

We consider the CoGaTI review is the best process for the AEMC to holistically consider the issues contributing to loss factor volatility and to formulate long-term access reform that will promote efficient and coordinated generation and transmission investment and allow participants to manage transmission-related risk.

In the short-term, we also support the AEMC's draft decision to provide AEMO with flexibility to refine the methodology for determining MLFs. This is in addition to other complementary reforms, already commenced, that will assist existing participants and new investors in predicting future changes to MLFs. Such reforms include the Transparency of New Projects rule change, as well as AEMO's plan to publish MLF data on a quarterly basis. This will enable market participants to better predict changes to their revenue as the result of future changes to MLFs, as well as enable improved locational decisions by investors.

We thank the AEMC for the opportunity to provide a submission to its draft rule determination. If you have any questions about our submission, please contact Arista Kontos (08 8213 3492).

Yours sincerely



Mark Feather
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Australian Energy Regulator