

Our Ref: 64584
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John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Submitted online via www.aemc.gov.au

Dear Mr Pierce

Request for change to the National Electricity Rules – monitoring and reporting of FCAS market performance

The Australian Energy Regulator (AER) is pleased to submit the attached rule change request to the Australian Energy Market Commission (AEMC).

Investor uncertainty about the viability of new conventional electricity generation investment, combined with recent coal plant closures, has contributed to a generation mix that is increasingly reliant on intermittent wind and solar energy. On the demand side, we have also seen a strong uptake of solar PV, storage and demand response.

Recognising the challenges arising from this transformation of the energy sector, in July 2016 the AEMC initiated its *system security market frameworks review*. The review focussed on addressing priority issues to allow the Australian Energy Market Operator (AEMO) to maintain power system security as the market transitions and made recommendations seeking to achieve this.

To progress several of these recommendations, in July 2017 the AEMC initiated its *frequency control frameworks review*. The recommendations were designed to address concerns about frequency performance in the National Electricity Market (NEM) and to consider how fast frequency control services offered by new technologies should be integrated into the current regulatory and market arrangements.

The purpose of this rule change proposal is to action recommendation three arising from the AEMC's frequency control frameworks review final report of July 2018.

Specifically, this recommendation seeks to place reporting requirements on the AER in relation to frequency control ancillary services (FCAS) market outcomes.

We consider that reporting on FCAS market outcomes aligns well with our formal responsibility to publish performance reports into the operation of the markets, retailer performance and the performance of the network businesses. We also include the results of such analysis in our State of the Energy Market reports.

For many years we have reported on FCAS costs for the NEM by service type as part of our Electricity Weekly reports and we make aggregated weekly cost data available on our website. We also have a statutory requirement under the rules to publish reports into FCAS prices above \$5000/MW and have published many reports in line with this requirement.

Further to this, we have a role under the National Electricity Law (NEL) to assess whether there is effective competition within a wholesale electricity market. This rule change proposal is consistent with this obligation.

Our rule change proposal differs slightly from what was suggested by the AEMC in its July 2018 final report. These changes are explained in detail in the attached rule change request.

We consider that this rule change proposal would satisfy the non-controversial test. The NEL defines a **non-controversial rule** as a rule that is unlikely to have a significant effect on the NEM. We consider that this rule change proposal would improve transparency of FCAS markets, and would therefore be beneficial, and without having any negative effects on the market. Further to this, stakeholders showed their support for this reporting requirement on the AER throughout the AEMC's consultation on the frequency control frameworks review.

Please contact Scott Hall on (08) 8213 3425 if you would like to discuss any aspect of this request.

Yours sincerely



Paula Conboy
Chair

National Electricity Rules
Monitoring and reporting of FCAS market performance

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1. Name and address of rule change proponent

Australian Energy Regulator
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Melbourne VIC 3001

AER reference: 63478
AER contacts: Gavin Fox, 02 6243 1249
Scott Hall, 08 8213 3425

2. Description of the proposed rule change

There is a range of ancillary services markets and a series of contracted services that ensure the secure operation of the power system. As the proportion of non-synchronous generation capacity increases, this may influence the performance and operation of FCAS markets.

This rule change request seeks to place reporting requirements on the AER in relation to FCAS market outcomes. The AER proposes, on a quarterly basis, to publish a report to include (as a minimum):

- the total costs of FCAS.
- volumes (both enabled and utilised), prices, number of participants for each of the eight FCAS markets and the technology types of those participants.
- commentary on key trends.

We consider that reporting on FCAS market outcomes aligns well with our formal responsibility to publish performance reports into the operation of the markets, retailer performance and the performance of the network businesses. We also include the results of such analysis in our State of the Energy Market reports.

Since the beginning of the NEM we have reported on wholesale market outcomes¹ in our Electricity Weekly reports, high price event reports², and in the statistics section of our website. Relevantly, we report on FCAS costs for the NEM by service type as part of our Electricity Weekly reports. In addition, our website contains weekly ancillary services costs data since January 2009. This proposed reporting requirement builds on this existing work.

Following amendments to the NEL in December 2016, we are required to monitor the wholesale market and report on its performance at least every two years. We are required to identify and analyse whether:

- there is 'effective competition' within the relevant wholesale market, as defined in the NEL.

¹ We also report on outcomes in the east coast gas markets.

² We have a statutory obligation to do this.

- there are features of the market that may be detrimental to effective competition within the market.
- there are features of the market that may be impacting detrimentally on the efficient functioning of the market and the achievement of the national electricity objective (NEO).

Our new role enables us to look more deeply into the way wholesale markets are operating to enhance market transparency and identify if there are impediments to competition or efficiency. It complements our existing monitoring of the wholesale markets, which largely have a shorter-term focus on compliance issues and high price events.

In December 2018 we published our inaugural report on wholesale electricity market performance.³ We assessed competition and efficiency in the FCAS markets using similar measures as for the spot market. As well as monitoring FCAS for the NEM as a whole, we focussed on FCAS issues in South Australia due to South Australia's high reliance on renewables and the fact that it often forms a regional market. Our report identified issues related to participant conduct in FCAS markets in South Australia, but concluded that it was unlikely that these issues would be sustained.

Significant trends in the market can manifest over comparatively short periods. It is important, therefore, that we analyse the markets looking across a range of timeframes in order to draw robust conclusions about market outcomes. This proposed quarterly reporting requirement for ancillary services fills the gap between weekly ancillary services costs data reporting and longer term trends in effectiveness of competition reporting. Similarly, the AER intends to commence quarterly wholesale electricity market reporting in 2019, potentially at the same time this requirement for quarterly FCAS market reporting comes into effect.

2.1 How our rule change proposal differs from the AEMC's drafting in the final report

While our rule change proposal is largely the same as was drafted by the AEMC in its frequency control frameworks review final report, we have made some changes, as follows.

Timing of reporting

As discussed elsewhere in this rule change request, we are in the process of re-evaluating the way we report on market outcomes. We currently publish Electricity Weekly reports (which contain FCAS costs for each service) and long term statistics on our website. We have for some time been considering adding quarterly reports on market outcomes to our suite of market reports. Importantly, this would allow us to incorporate our observations and analysis across the electricity spot market, FCAS markets, electricity contract markets and gas markets into one publication.

So, the requirement to prepare and publish a report in respect of each quarter into FCAS market outcomes aligns well with our vision for reporting on wholesale market outcomes.

³ For our 2018 report we focused primarily on the regional spot energy markets. We also analysed the frequency control ancillary services (FCAS) markets and considered the implications of the contract markets and incentives offered under the renewable energy target scheme where relevant.

However, our experience with preparing and publishing monitoring reports tells us that complex market outcomes can, on occasion, take some time to analyse. To this end, rather than placing an obligation on ourselves to publish a report four weeks from the end of the relevant quarter, we propose instead to not impose any such hard time limit on ourselves, but rather to make the reports available as soon as practicable from the end of the relevant quarter. This would allow us to undertake fulsome analysis of complex and potentially interrelated market outcomes. However, to ensure the market is provided with timely information, in addition to producing quarterly reports, we propose to update cost and price information in the statistics section on our website on a regular basis.

Assessment of effectiveness of competition

An important area where our proposed rule differs from the suggested drafting in the AEMC's final report is in respect of us assessing whether the FCAS markets are functioning efficiently and whether there is effective competition.

As discussed elsewhere in this rule change proposal, under the NEL we are required to monitor the wholesale market and report on its performance at least every two years. As part of this, we are required to identify and analyse whether there is 'effective competition' within the relevant wholesale market. We have done this for the FCAS markets (with a focus on South Australia) as part of our inaugural report into effective competition. We consider, for completeness and to maintain consistency, it makes sense to continue to consider all relevant wholesale markets (including FCAS) as part of our ongoing review into the effectiveness of competition in those markets. In this way, we will meet the AEMC's intent that we report on the effectiveness of competition in FCAS markets.

To this end, we have removed the AEMC's proposed clause 3.11.2A(4) from our proposed drafting.

Clause to capture possible future analysis

Finally, we have added the words "any other relevant information the AER considers should be included" in number 4 of the proposed drafting (see Attachment 1) to indicate we remain committed to analysing and reporting on emerging trends in the FCAS markets in light of technological developments.

2.2 Background to the rule change request

Investor uncertainty about the viability of new electricity generation investment, combined with recent coal plant closures, has contributed to a generation mix that is increasingly reliant on intermittent wind and solar energy. On the demand side, we have also seen a strong uptake of solar PV, storage and demand response.

This transformation presents both opportunities and challenges for power system security. The AEMC and the Finkel Panel (amongst others) have previously identified the system security challenges associated with the transformation of the energy sector.

Recognising the challenges arising from this transformation of the energy sector, in July 2016 the AEMC initiated its system security market frameworks review. The review focussed on addressing priority issues to allow AEMO to maintain power system security as the market transitions and made recommendations seeking to achieve this.

To progress several of these recommendations, in July 2017 the AEMC initiated its frequency control frameworks review. The recommendations were designed to address concerns about frequency performance in the NEM and to consider how fast frequency control services offered by new technologies should be integrated into the current regulatory and market arrangements.

The purpose of this rule change proposal is to action recommendation three arising from the AEMC's frequency control frameworks review final report of July 2018. Specifically, this recommendation seeks to place reporting requirements on the AER in relation to FCAS market outcomes.

3. Statement of issues

FCAS market dynamics have changed recently with the entry of new providers, and changes in the types of technologies providing FCAS. By implementing the changes in this rule change proposal, interested stakeholders will be assured of ongoing access to price, cost and other relevant FCAS markets information to allow them to understand the costs involved in meeting the requirements of the frequency operating standard and to help stakeholders make investment and operational decisions.

4. How the proposed rule contributes to the National Electricity Objective (NEO)

Under section 7 of the NEL, the NEO states:

“The objective of this Law is to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to

- (a) price, quality, safety, reliability and security of supply of electricity
- (b) the reliability, safety and security of the national electricity system.”

We consider the relevant aspects of the NEO for the purposes of this rule change request are the efficient investment in, and operation of electricity with respect to the price and security of supply of electricity, as well as the safety and security of the national electricity system.

5. Expected benefits and costs associated with the proposed rule

We consider that the benefits of us providing the information required by this rule change proposal outweighs the costs involved, given that we already report on most of the information required in our Electricity Weekly reports and on our website, and we already have a requirement under the NEL to report on the effectiveness of competition in the wholesale markets.

We consider that one of the benefits of having a formal reporting requirement in the rules in relation to the FCAS markets would be to ensure that stakeholders and policy makers have access to FCAS markets data on an ongoing basis.

Specifically, stakeholders would have ongoing access to costs to meet frequency requirements, and, given that we would report on costs and prices on an ongoing basis, stakeholders would have access to trend information that may be useful in making investment and operational decisions. Access to FCAS cost and price information would also help inform policy.

Attachment 1 – Draft Rule

3.11.2A Reporting on market ancillary services markets

- (a) The AER must prepare and publish a report in respect of each three month period commencing on 1 January, 1 April, 1 July and 1 October in each year. The report must:
1. be published as soon as practicable after the end of the relevant three month period and must contain:
 - a) the total costs for the provision of that market ancillary service for each region;
 - b) the total quantity of that market ancillary service enabled by AEMO in each region;
 - c) the total quantity of that market ancillary service utilised by AEMO in each region;
 - d) the average, lowest and highest ancillary service price for each region for that market ancillary service; and
 - e) the number and types of ancillary service providers;
 2. contain the following information in relation to each market ancillary service listed in clause 3.11.2(a) for that three month period:
 3. contain the AER's analysis of key trends in the market ancillary service markets over that three month period; and
 4. contain any other relevant information the AER considers should be included.