

24 August 2022

Ms Jenness Gardner
Chief Executive Officer
Economic Regulation Authority
Email: publicsubmissions@erawa.com.au

Dear Ms Gardner,

Triennial Review of the Effectiveness of the Wholesale Electricity Market 2022

Thank you for the opportunity to comment on the Economic Regulation Authority's (ERA) Triennial Review of the Effectiveness of the Wholesale Electricity Market 2022 Discussion Paper (the Discussion Paper). I acknowledge that the ERA has chosen to take a forward-looking approach to this review, which the Australian Energy Market Operator (AEMO) agrees provides a useful approach in the context of the significant changes to the Wholesale Electricity Market (WEM) arrangements scheduled to commence from October 2023, and the challenges and opportunities arising from the advancement of sectoral decarbonisation.

AEMO has a central role in convening efforts to enable an orderly energy transition to net zero, while ensuring power system security and reliability is maintained. As such, AEMO is deeply involved in the Western Australian Government's broader energy reforms to deliver improvements to the design of the WEM and South West Interconnect System (SWIS).

These reforms include a range of initiatives, several of which are thoroughly considered within the ERA's Discussion Paper. Some notable additions include the Distributed Energy Resources (DER) Roadmap, which is developing and implementing measures to improve visibility and control of DER, as well as technical and market frameworks to enable DER to participate in the future electricity system and be compensated for these services. The WEM reform program is also implementing a range of measures to help provide for emerging system operation needs, including the development of market frameworks to support the participation of flexible technologies, improving generator performance standards, and updating technical standards underpinning the operation of the power system.

AEMO believes that the challenge of operating a net zero emissions power system will involve a suite of complementary initiatives, the contribution of which each in isolation is challenging to measure. A key limitation of all modelling undertaken to-date is that, by necessity, it cannot be informed by practical experience in managing the SWIS with only renewable energy. As the party responsible for the management of the system, AEMO is on the forefront of the transition and is evolving its systems and processes to enable the operation of the system with declining levels of thermal generation. This includes learning from the practical experience of running a net zero emissions power system on renewable energy for short periods of time, which AEMO expects to be doing by 2025. In this transition it is important that current generation technologies are not displaced before suitable replacements are imbedded in the operation of the power system.

As the Discussion Paper highlights, with the SWIS decarbonising in response to Government targets, more renewable generation will be needed to replace thermal generation. As most renewable generation is weather-dependent, technologies (such as storage) will need to be available to manage intermittency as well



as provide essential system services. In addition to storage, AEMO believes the management of DER can play an important role in providing these services. The above-mentioned DER work program is an example of the work that is being undertaken, in collaboration with our industry partners, to achieve this.

One of the challenges outlined in the Discussion Paper is the low operational cost of renewables, in the context of the current market settings, that will likely lead to lower prices in the energy market. This may result in a deficiency of signals to invest in replacement generation, including flexible capacity. While there are market settings to allow for the procurement of additional capacity and essential system services, these are not intended for regular use. That is, an over-reliance on such settings is not conducive to a healthy market.

The work of the review into the Reserve Capacity Mechanism (RCM Review) is going some way to addressing the matter of flexible capacity requirements. While the ERA's concerns that the RCM Review's preliminary findings are unlikely to fully account for the revenue sufficiency problem outlined in the Discussion Paper, AEMO notes that the RCM Review is about to begin a public consultation process, with input from industry (including the Discussion Paper) to inform the final recommendations for implementation in 2023.

AEMO also notes that the recently announced draft Ministerial Statement of Policy Principles outlines a high-level Government proposal to implement an incentive regime that encourages new investment in flexible capacity, to be funded through a penalty on new and incumbent high-emissions generation. The findings of the Discussion Paper are opportunely timed to inform the design of the scheme, which AEMO understands will be incorporated into the RCM Review.

A key element that is not currently explored within the high-level outline of the draft Ministerial Statement of Policy Principles and the RCM Review, is potential for energy markets to respond to the emerging issues outlined in the Discussion Paper. While AEMO expects that the capacity market can play a role in providing the appropriate price signals to encourage new investment, the RCM will be one of several mechanisms required to fully address the challenges ahead in an economically efficient manner.

The Discussion Paper outlines three questions for industry feedback. The first two questions relate to the matters being explored as part of the RCM Review, including actions resulting from the draft Ministerial Statement of Policy Principles. AEMO intends to respond as part of the RCM Review's consultation process, which will allow for feedback to be provided in the context of the broader elements of the review. The final question relates to locational pricing, which the advantages and disadvantages were discussed during early design stages of the reform program. Notwithstanding, AEMO notes that such a change would require considerable work to implement and should be subject to a robust cost benefit analysis to inform decision making.

AEMO stands ready to assist policy makers and the market in understanding the transition ahead, and thanks the ERA for its forward-looking review of the effectiveness of the WEM which we believe provides a valuable contribution to meeting this challenge.

Yours sincerely,



Martin Maticka

Group Manager – WA Development