



19 September 2018

Attn: Mr Matthew Martin
Director, Wholesale Energy Markets
Public Utilities Office
Department of Treasury
Locked Bag 11
Cloisters Square WA 6850

By email: PUOSubmissions@treasury.wa.gov.au

Dear Matthew

Draft Recommendations Report – Improving Reserve Capacity Pricing Signals

Alinta Sales Pty Ltd (**Alinta**) welcomes the opportunity to provide a submission to the Public Utilities Office (**PUO**) on its Draft Recommendations Report: Improving Reserve Capacity Pricing Signals (**draft recommendations report**).

Alinta commends the PUO on its approach to developing the draft recommendations report and has appreciated the opportunity it has had to engage with the PUO on the detail prior to the release of the report for written submissions.

Alinta is an active investor in energy markets across Australia with an owned and contracted generation portfolio of nearly 3,000MW, including its Pinjarra and Wagerup Power Stations in the South West Interconnected System (**SWIS**). Alinta has a detailed renewable investment strategy and is pursuing renewable energy projects at an increasing scale. Alinta currently retails electricity and gas to more than 1,000,000 customers nationwide and is committed to contributing to energy market development across Australia.

The diversity of Alinta's portfolio, its investment strategy, product offerings, and first-hand experiences across multiple jurisdictions has allowed it to develop a detailed understanding of wholesale electricity markets across Australia and various policies designed to incentivise investment. Alinta is therefore well placed to provide informed comment in response to the PUO's draft recommendations report.

1. Introduction

The underlying conditions that resulted in the adoption of a capacity mechanism in the SWIS included its isolation, small size, lumpy demand, load shape, large market concentration and high level of State Government ownership. These characteristics have not changed since the initial decision by the State Government at the time regarding the Wholesale Electricity Market (**WEM**) design, but rather continue to mean that the SWIS is relatively unique when compared to other similar electricity markets around the world.

Alinta considers that the original drivers for the inclusion of a capacity mechanism in the WEM continue to remain relevant and that the remaining question is whether to maintain the current approach of using an administered pricing mechanism or to adopt an alternative approach.

Alinta supports retaining, and refining, the current administered pricing mechanism and is pleased to see the PUO's recommendations to this effect.

2. Price Cap and Floor

Alinta supports the proposal to include a CPI escalated price cap and floor into the Reserve Capacity Price (**RCP**) formula for existing capacity providers. This approach minimises sovereign risk by recognising the long-term investment decisions made by existing capacity providers under the regulatory framework at the time those decisions were made. Further, the proposed price tranche will ensure an element of revenue certainty for existing investments while not distorting the signals provided to new entrant capacity.

While not explicitly addressed, Alinta assumes that any efficiency measures or upgrades made to existing generation facilities, which result in an increase of capacity credits allocated, will be remunerated within the cap and floor.

Noting the support for the concept of the price cap and floor, Alinta is concerned that the proposed values will provide below expectation commercial returns on investment. To ensure the ongoing commerciality of projects which are already in operation, Alinta recommends that the proposed price floor be amended to \$110,000/MW. Alinta considers that this would also be closer to the level where existing capacity providers could secure refinancing. Further to this, Alinta questions whether the upper band should also be adjusted such that the forecast capacity outcomes in later years (as outlined in the draft recommendations report) fall within the price tranche.

3. Treatment of Demand Side Management

In the WEM, Demand Side Management (**DSM**) is likely to be the lowest fixed cost capacity to enter the market. Given this, there needs to be sufficient measures in place to encourage the efficient and appropriate entry of DSM. However, Alinta is concerned about the risk of significant levels of DSM entering the market (as seen in previous eras) and the resultant impact of depressing the existing generator's RCP to the floor throughout the transitional period.

Given this, Alinta is strongly of the opinion that a number of mechanisms are required to ensure that DSM is a "real" and useable product for the market to utilise and is therefore treated as closely to conventional generation as possible. To that end, Alinta supports the PUO's proposal for:

- enhanced annual security obligations for DSM; and
- enhanced testing obligations by including truly random Reserve Capacity Tests.

In addition to the above, Alinta recommends that the PUO consider inclusion of the following additional reforms:

- Development of an annual limit on the maximum DSM to be procured in a Reserve Capacity Year;
- Limits on oversubscription of loads in a DSM program to bring the performance risk of DSM to be more in line with conventional generation; and

- reforms to dispatch arrangements to ensure DSM can be, and is, dispatched (rather than dispatching diesel generators first).

These additional reforms, coupled with the PUO's proposal, will ensure that DSM is a useable product while also ensuring that only efficient and appropriate levels of DSM are encouraged to enter the market.

4. Conclusion

Alinta supports retaining, and refining, the current administered pricing mechanism to incentivise the efficient entry and exit of capacity. Subject to the consideration of the minor enhancements to the proposal, as outlined in this submission, Alinta supports the PUO's recommendations.

Please contact me on Jacinda.Papps@alintaenergy.com or 08 9486 3009 if you have any queries in relation to our comments on the proposal.

Yours Sincerely

Jacinda Papps
Manager, National Wholesale Regulation