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## Wholesale Electricity Market Submission to Procedure Change Proposal

**PC\_2011\_06      5-yearly Review of the Methodology and Process  
for Determining the Maximum Reserve Capacity  
Price**

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### Submitted by

<b>Name:</b>	Corey Dykstra
<b>Phone:</b>	08 9486 3406
<b>Fax:</b>	08 9221 9128
<b>Email:</b>	corey.dykstra@alinta.net.au
<b>Organisation:</b>	Alinta Sales Pty Ltd
<b>Address:</b>	12-14 The Esplanade PERTH WA 6000
<b>Date submitted:</b>	4 October 2011

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### Submission

Clause 2.10.7 of the Wholesale Electricity Market Amending Rules provides that any person may make a submission for a Procedure Change Proposal by filling in this Procedure Change Submission form.

Submissions for Procedure Changes that relate to the Power System Operation Procedures and IMO Market Procedures should be submitted to:

#### **Independent Market Operator**

Attn: Manager Market Development & System Capacity  
PO Box 7096  
Cloisters Square, Perth, WA 6850  
Fax: (08) 9254 4399  
Email: market.development@imowa.com.au

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**1. Please provide your views on the Procedure Change Proposal, including any objections or suggested revisions:**

#### **Background**

The Maximum Reserve Capacity Price (MRCP) Market Procedure (the Market Procedure) details the method and process to be followed by the IMO in annually determining the MRCP. Clause 4.16.9 of the Market Rules also requires that the IMO review the Market Procedure at least once in every five year period.

To assist the IMO in the current five year review, a working group of the Market Advisory Committee (MAC), the MRCP Working Group (the Working Group), was established to consider, assess and develop any necessary change to the Market Procedure.

#### **Procedure Change Proposal**

The amendments to the Market Procedure proposed by PC\_2011\_06 would make a number of changes to the method for determining the MRCP. These changes are consistent with those generally considered appropriate by the Working Group.

#### **Alinta's views**

Alinta was represented on the Working Group, and is generally comfortable with the rationale for the changes proposed by PC\_2011\_06 to the method outlined in the Market Procedure for determining the MRCP.

Nevertheless, the IMO's analysis shows that had the revised method been used to establish the MRCP for the 2013/14 Capacity Year, the resultant MRCP would have been around 24 per cent lower than using the existing method set out in the Market Procedure.

As a matter of general principle, it may be prudent to provide for a transition period where a change in method, as opposed to a change in the observed value of input parameters, results in material changes in financial flows between Market Participants.

Providing for a transition period would appear especially appropriate in instances, such as in respect of the amendments being contemplated by PC\_2011\_06, where the changed method immediately changes financial flows between market participants, but where due to fixed term contracts, benefits can only be expected to flow through to customers over time.

For example, it may be appropriate to provide for a transitional mechanism to smooth the financial impact of any changed methodology where the outcome would otherwise result in changes that exceed a certain threshold level - say ±10%.

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**2. Please provide an assessment whether the Procedure Change Proposal is consistent with the Market Objectives and the Wholesale Electricity Market Amending Rules.**

Market Rule 2.9.3 states that the Market Procedures, as proposed to be amended or replaced, must be consistent with the Wholesale Market Objectives. The Wholesale Market Objectives are as follows.

- (a) to promote the economically efficient, safe and reliable production and supply of electricity and electricity related services in the South West interconnected system;
- (b) to encourage competition among generators and retailers in the South West interconnected system, including by facilitating efficient entry of new competitors;
- (c) to avoid discrimination in that market against particular energy options and technologies, including sustainable energy options and technologies such as those that make use of renewable resources or that reduce overall greenhouse gas emissions;
- (d) to minimise the long-term cost of electricity supplied to customers from the South West Interconnected System; and
- (e) to encourage the taking of measures to manage the amount of electricity used and when it is used.

The primary purpose of the MRCP is to cap the price that may be paid by the IMO if insufficient capacity is made available to the market voluntarily and the IMO is therefore required to procure additional capacity through a Reserve Capacity Auction.

However, the MRCP also links to the price paid for capacity that is voluntarily provided to the market, but is not bilaterally traded – the Reserve Capacity Price is set to 85% of the MRCP and further adjusted to account for any over supply of capacity.

Although this linkage was not within the scope of the review of the MRCP (and it is noted that the IMO Board has commissioned a separate review of the Reserve Capacity Mechanism), Alinta considers that as a matter of general principle, it would be prudent to provide for a transition period where a change in method, as opposed to a change in the observed value of input parameters, results in material changes in financial flows between Market Participants.

Given the linkage between the MRCP and the price paid for uncontracted capacity, Alinta is concerned that the step change in the MRCP that would result from the proposed change in the method for determining the MRCP contemplated by PC\_2011\_06, rather than in the observed value of input parameters, may increase the perceived regulatory risk associated with investments in the Wholesale Electricity Market (WEM).

To the extent that the changes contemplated by PC\_2011\_06 increase the perceived regulatory risk associated with investments in the WEM, the efficient entry of new generation competitors may be impeded. In addition, it is likely that existing generators would attribute a lower risk-adjusted value to the revenue stream from Capacity Credits, which would lead to increased energy costs for retailer.

Consequently, the additional risk perceived to be associated with participating in the WEM may increase the long-term cost of electricity supplied to customers from the South West Interconnected System.

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**3. Please indicate if the Procedure Change Proposal will have any implications for your organisation (for example changes to your IT or business systems) and any costs involved in implementing these changes.**

The changes to the Market Procedure contemplated by PC\_2011\_06 would not require Alinta to change its IT or business systems, and hence there are no IT or business costs associated with the Rule Change Proposal.

As noted earlier, PC\_2011\_06 would materially change financial flows between market participants. As a net provider of capacity to the WEM, the changes proposed by PC\_2011\_06 would result in a material reduction in Alinta's revenue, which overtime would likely be recovered through higher prices to customers.

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**4. Please indicate the time required for your organisation to implement the changes, should they be accepted as proposed.**

The changes to the Market Procedure contemplated by PC\_2011\_06 would not require Alinta to change its IT or business systems, and hence there is no specific period of time that would be required to implement the changes arising from the Procedure Change Proposal.

However, as noted earlier, it may be prudent to provide for a transition period where a change in method, as opposed to a change in the observed value of input parameters, results in material changes in financial flows between Market Participants.

For example, it may be appropriate to provide for a transitional mechanism to smooth the financial impact of any changed methodology where the outcome would otherwise result in changes that exceed a certain threshold level - say ±10%.

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