

4 May 2018

Matthew Martin
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Public Utilities Office
Department of Treasury

Email: PUOSubmissions@treasury.wa.gov.au

RE: Improving Reserve Capacity pricing signals – alternative capacity pricing options consultation Paper

Thank you for the opportunity to provide comment on the Improving Reserve Capacity pricing signals consultation paper. Change Energy is a new electricity retailer in WA. Our objective is to use our expertise in electricity markets, solar PV, energy efficiency and new technologies to give small businesses sustainable lower electricity costs.

The following are general comments on Reserve Capacity pricing:

1. Change Energy supports an administered capacity pricing approach. This approach provides stability and certainty to both customers and generators which should provide lower cost outcomes over the long-run. It has been our long-standing view that under the original market rules, excess capacity is not an extra cost to customers. Once the Reserve Capacity Target (RCT) and the Benchmark Reserve Capacity Price (BRCP) is set, the product of the RCT x the BRCP is the amount that customers will pay for Reserve Capacity for that year. Under the original market rules, the Reserve Capacity Price (RCP) was adjusted to account for any excess capacity that was assigned (the -1 slope). Contestable customers have been paying for the total Reserve Capacity cost through both targeted and shared reserve capacity costs based on the RCP since competition began.
 2. Any form of Reserve Capacity pricing that is developed to proxy a competitive pricing outcome will inherently become a highly administered process. This is due to the fact that the WA market is small with very few participants and one large dominant government owned entity. The number and complexity of the additional rules that would be required to mitigate market power will lead back to an administered price. And with all of the additional rules the risk of unintended consequences increases with potentially devastating impacts to market participants. This would apply both to any type of auction process or retailer-led contracting method for procuring capacity. Change Energy does not support these proposals.
 3. Change Energy believes that the Reserve Capacity mechanism should be used to incentivise new capacity into the market to ensure there is enough to meet reliability targets. It should not be used as a tool to try make existing capacity leave the market. Markets off all types around the world have demonstrated that once capacity has been installed, it will stay in the market until the end of its useful life. The economic value of the capacity will change over time and investors will bear this risk. Existing capacity will always be revalued by new investors to ensure that there is a return to be made.
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4. Increasing the volatility in setting the Reserve Capacity price will increase the price. Investors will demand a higher return on their investment that is consistent with the higher risk to the price. The WACC calculations that feed into setting the Reserve Capacity price will need to account for the higher risk premium.
5. Change Energy supports Demand Side Management (DSM) being included in the Reserve Capacity mechanism. The current approach of applying a different price to DSM capacity is acceptable for the interim, however a more holistic approach is needed.
6. Change Energy believes that a wider review of the Reserve Capacity Mechanism is urgently required to ensure that the future of the electricity system remains stable and is set up to provide customers with the lowest possible costs driven by competition.

Change Energy would be happy to meet with the PUO to discuss the issues raised in our submission.

Yours Sincerely,

A handwritten signature in black ink, appearing to read "G. Gaston".

Geoff Gaston

Chief Executive Officer

