

21 September 2018

Mr Ashwin Raj
Manager, Energy Networks
Public Utilities Office
Department of Treasury
David Malcolm Justice Centre
28 Barrack Street
PERTH WA 6000
ashwin.raj@treasury.wa.gov.au

Response to Consultation Paper: Proposed approach to implement constrained network access

1. Introduction

Merredin Energy Pty Ltd (**MEPL**) owns and operates the 82 MW open cycle gas turbine power station located in Merredin, Western Australia. The financial performance of the plant is highly dependent on the revenue earned by providing Capacity Credits under the Reserve Capacity Mechanism (**RCM**). Proposed reforms that change network access arrangements, capacity certification processes and Reserve Capacity Prices (**RCP**) have the potential to significantly impact the profitability of the Merredin Plant.

Given the above, we have a significant interest in proposed reforms and provide this submission to ensure that the policy makers consider the impact of proposed reforms on existing Market Participants and put in place new arrangements that ensure sufficient dispatchable generation capacity remains in the market to ensure a reliable and secure electricity system in the South-West of Western Australia.

2. Merredin Energy's concerns with constrained network access

As outlined in our submission to the Public Utilities Office (**PUO**) on constrained network access (23 March 2018), MEPL is concerned that the loss of firm network access rights for existing generators would act as a barrier to future investment in dispatchable generation in the South West Interconnected System (**SWIS**).

Investment cases for new generation plant in the SWIS have been based on managing operational and market risks, while network risks were negligible. By adding network access risks under constrained access, investors and debt providers will require significant premiums if investing in generation assets that have operating lives up to and exceeding 30 years. Understanding the likely future mix of generation plant over 30 years (or even 80 years as outlined in the PUO modelling of constrained access) and determining the likely future constraints imposed on existing generation is almost an impossible task – which results in the

determination of appropriate financial compensation amounts for affected parties becoming extremely difficult. The future generation mix in the SWIS will be a function of National emission reduction targets (which are highly uncertain to 2030 and beyond), future WA Government schemes to reduce emissions (if any), and the economics of different and emerging technologies (e.g. battery storage, solar and wind technologies).

Given the difficulty of determining financial compensation for existing generators, MEPL's strong preference is that existing rights for incumbent generators should be maintained and that constrained access should only apply to new facilities. However, the PUO modelling indicates that partially constrained network access is the most expensive option and has recommended that fully constrained network access be introduced for all generators from 2022.¹

3. Proposed Approach to implementing constrained access

The PUO has re-iterated in the most recent discussion paper (August 2018) that financial compensation will be provided to incumbent generators that are disadvantaged by the implementation of constrained network access.

The approach to providing financial compensation involves the following steps:

- Creation of financial rights for incumbent generators. This involves converting the right to physically transmit energy across the network on an unconstrained basis with a financial right to receive a payment in lieu of being able to do so. These financial rights would be grandfathered, retaining effect until a defined trigger point (which the PUO is seeking comment on)
- Provision of transitional assistance to incumbent generators that are disadvantaged by the transition to constrained network access
- Calculation of the amount of transitional assistance that should be paid to disadvantaged generators. The PUO will conduct "One on One" meetings with affected generation facilities (as requested by MEPL and other Market Participants in the previous round of submissions) to help understand the likely impact on participants from detailed modelling carried out by EY

3.1 Creation of Financial Access Rights

It is proposed that MEPL's physical rights to the Western Power (**WP**) network will be replaced with financial rights. A scheme would be established to provide this assistance (**the Scheme**). While we acknowledge that the scheme is in the early stages of development and will be subject to further industry consultation, we make the following points.

- MEPL is willing to register for the scheme and disclose its access contract to parties responsible for administering the Scheme (subject to keeping the information strictly confidential)
- MEPL would agree to a set of terms and conditions for changing firm access rights under the Scheme, subject to review by MEPL, legal counsel and energy consultants. It is paramount that the terms and conditions are consistent across all generators participating in the Scheme to ensure that constrained access is implemented fairly
- The current network access contracts are likely to expire well before the end of generator's economic plant life. For example, the Merredin Energy plant is expected to continue in service until 2037. Transitional assistance should not be based on the term of the Electricity

¹ Public Utilities Office, Department of Treasury, Improving access to the Western Power Network, Proposed approach to implement constrained network access, 9 August 2018, Executive Summary p.VI.

Transfer Access Contract (**ETAC**) but should be based on the likely retirement date for the plant. The initial investment decision to finance and develop the Merredin plant was based on firm and unconstrained access to the WP grid for the plant's life, not for the term of the ETAC

3.2 Statutory Immunity for WP

The PUO is proposing that WP will receive statutory immunity from inconsistencies in the terms and conditions of current access contracts and constrained access reforms. That is, WP will be protected from failing to provide a level of physical access in accordance with contractual conditions under ETAC.

It is MEPL's view that a limited immunity for breaching contractual conditions should be put in place and must relate to terms and conditions that limit the application of constrained access on existing generators. All other conditions should be subject to commercial negotiation with WP and should be undertaken with no statutory immunities in place. This is required to provide a balance between WP and parties renegotiating access conditions (including derogations from technical standards).

3.3 Managing Transitional Assistance

The PUO proposes that transitional assistance will be managed via an administered solution (as opposed to a market mechanism outlined in the previous discussion paper in March 2018). Under this approach, the PUO will enter direct negotiations and be responsible for compensation payments to affected generators. This was MEPL's preferred approach and we welcome upcoming discussions and negotiations to implement constrained access in a fair and equitable way.

We appreciate that the quantum of transitional assistance would be based initially on the individual generator's results under the EY market modelling that has been commissioned by the PUO. MEPL will also need to commission its own market modelling to independently verify the EY modelling results and to consider scenarios not modelled by the PUO. As outlined earlier, predicting the future generation mix in the SWIS over the next 20 years and how that impacts the network access for an individual generator has high uncertainty and will require a detailed and comprehensive scenario approach to understand the likely range of outcomes.

Part of the discussion with the PUO will be how the transitional assistance for implementing constrained access will interplay with proposed capacity market reforms. That includes the concept of "capacity priorities" for incumbent generators that was outlined in an earlier discussion paper.² For example, does the implementation of "capacity priorities" reduce transitional assistance provided to affected generators under the scheme?

4. Timeframes for Implementation

Given the significance of the changes, time required for negotiations with WP on network access and the WA Government on transitional assistance, as well as time to develop new business plans for incumbent generators (typically operating on 5-year strategic plans), it is our preference that implementation would occur on October 2023 and not October 2022 as proposed.

² Public Utilities Office | Department of Treasury, Allocation of capacity credits in a constrained network, 26 February 2018



Regards,

A handwritten signature in black ink that reads 'J. Delicato'. The signature is written in a cursive style with a large initial 'J' and a distinct 'D'.

John Delicato
General Manager
Merredin Energy