

02<sup>th</sup> February 2016

Simon Middleton  
Public Utilities Office, Department of Finance  
Level 1, Albert Facey House  
469 Wellington Street  
Perth WA 6000

Dear Simon,

**Submission: Reserve Capacity Mechanism Position Paper Response – TransAlta**

TransAlta has reviewed the position paper containing suggested reforms to the Reserve Capacity Mechanism (**Position Paper**), as issued by the Public Utilities Office in December 2015 and welcomes the opportunity to make comment on the proposed changes.

TransAlta Energy (Australia), through its various subsidiary companies and partnerships, is an active capacity supplier under the Reserve Capacity Mechanism.

TransAlta is supportive of the objectives and principles outlined in the Position Paper and of the general outcomes that have been proposed in the Position Paper. We would like to make a number of comments on specific parts of the changes that have been proposed in the hope we can make a positive contribution to the reform discussion.

Slope of the Reserve Capacity Price Formula during Transition Period

*PUO Proposal:* To steepen the slope of the capacity price formula from negative 1 to negative 5 for the transition period.

*Comment:* The objectives of this reform include providing the appropriate market signals/incentives to drive the efficient retirement of plant and the removal of capacity in times of oversupply. We believe that Synergy is the Market Participant most likely to be able to efficiently respond to the current capacity oversupply signals. We expect Synergy is able to do so because of the size, composition and age of its generation fleet. Should a reduction in the levels of excess capacity not eventuate, then even with the expected reduction of 220 MW of demand side management capacity, the negative commercial implications for other generation-base Market Participants, who are comparatively less responsive to market signals, may be significant.

The move to the proposed slope of negative 5 appears to be a departure from the recommendation by the Lantau Group to use a slope of negative 3.75 in previous work commissioned by the IMO (now AEMO). The Lantau Group recommendation followed a comprehensive and consultative review of the design and performance of the Reserve Capacity Mechanism and no quantitative justification for a shift to a negative 5 slope has been offered through the current reform process.

TransAlta supports a negative 3.75 slope as originally proposed by the Lantau Group.

### Constant Slope Vs Sequentially Increasing the Slope during the Transition Period

*PUO Proposal:* Maintain a constant slope for the duration of the transition period.

*Comment:* There exists a risk that the current reform process does not result in a sufficient quantity of capacity being removed from the market. The resultant price shock in the market would then be an unintended outcome of the reform process. To mitigate this risk, TransAlta is supportive of a phased transition approach, as mentioned in the Position Paper (pp. 46), whereby the slope of the curve is increased sequentially so as to become more aggressive over time. TransAlta would be supportive of sequentially increasing the slope to negative 3.75 over a period of 5 years. This approach would enable businesses to better deal with the cash flow implications of the changes that are being adopted.

### Trigger for First Auction

*PUO Proposal:* To either set a drop-dead date for the first capacity auction or wait until the market has reached an acceptable level of balance, deemed to be when there is approximately 5 – 6 % excess capacity.

*Comment:* Holding an auction before the market is balanced runs a high-risk of causing disruption to all parties involved. TransAlta is supportive of waiting until the 5 – 6 % excess level is reached. If the proposed transition measures do not have the desired effect of reducing levels of excess capacity, then these measures should be revisited as a first course of action in order to mitigate against market shock.

### Dynamic Refund

*PUO Proposal:* To implement a dynamic capacity refund regime to reflect the economic value of not making capacity available to the market.

*Comment:* The capacity refund formula is centered around two inflection points of 750 MW and 1500 MW excess capacity. These inflection points correspond to a refund multiplier of 6 and 0.25 respectively, but are in fact static in nature. That is, the inflection points do not allow for an expansion or contraction in the size of the market in total (and hence the margins needed for outage planning purposes). TransAlta is concerned that the parameters proposed resulted from analysis conducted prior to the current reform process and there may be cumulative effects that have not been fully considered.

If the other measures proposed in the Position Paper have the desired effect of reducing the level of excess capacity in the market, then higher multipliers are likely to apply for a higher percentage of time. The basis for setting the inflection points is unclear and they appear to have been arbitrarily set. Therefore, there exists the potential that the combined effect of removal of capacity from the market will influence the overall level of refunds ultimately paid by those remaining in the market.

TransAlta requests consideration of, and confirmation that, the assumptions used to determine refund parameters will remain appropriate should the other reforms have the desired effect of reducing the excess capacity.

If you have any questions regarding this submission please contact me on 9420 0628.

Yours sincerely,

**Troy Forward**  
Commercial Manager