



**Draft Rule Change Report
Title: Eligible Services for
Supplementary Reserve Capacity**

Ref: RC_2008_28

Standard Rule Change Process

Date: 21 November 2008

CONTENTS

1.	INTRODUCTION	2
2.	THE RULE CHANGE PROPOSAL.....	3
2.1.	Submission Details.....	3
2.2.	Details of the Proposal	3
2.3.	The Proposal and the Wholesale Market Objectives	4
2.4.	Amending Rules proposed by the IMO	4
2.5.	The IMO's Initial Assessment of the Proposal	5
3.	SUBMISSIONS	6
3.1.	Public Forums and Workshops	6
3.1.1	Supplementary Reserve Capacity Working Group	6
3.1.2	Market Advisory Committee	7
3.2.	Submission from LGP	7
3.3	Submission from Synergy	8
3.3	Submission from Alinta.....	8
4.	THE IMO'S ASSESSMENT AND DECISION	9
4.1.	Assessment.....	9
4.2.	IMO's Draft Decision	10
5.	CALL FOR SUBMISSIONS	11
6.	PROPOSED AMENDING RULES.....	12
7.	GENERAL INFORMATION ABOUT RULE CHANGE PROPOSALS	13

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Independent Market Operator

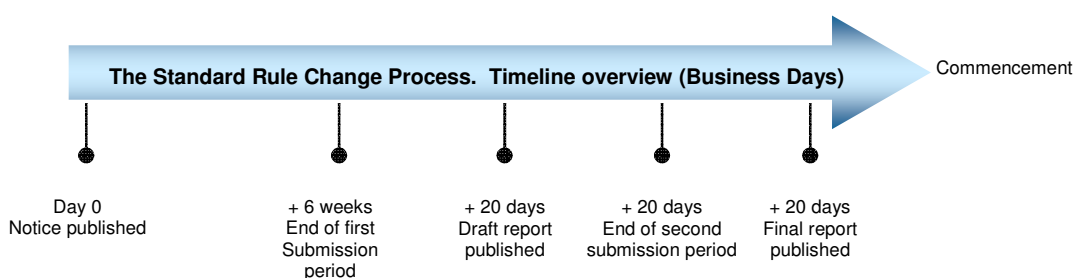
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1. INTRODUCTION

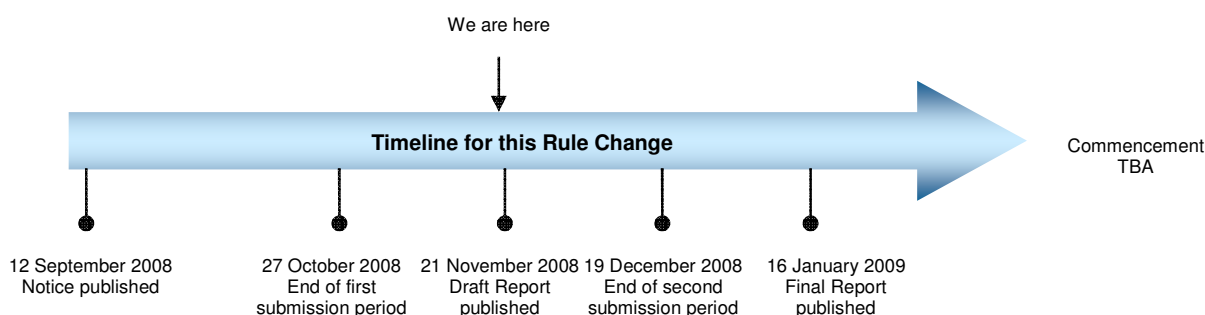
On 11 September 2008 the Independent Market Operator (IMO) submitted a Rule Change Proposal regarding changes to clauses 4.24.3 and 4.24.15 of the Wholesale Electricity Market Rules (Market Rules).

This Proposal is being processed using the Standard Rule Change Process, described in section 2.7 of the Market Rules.

The standard process adheres to the following timelines, outlined in section 2.7 of the Market Rules:



The key dates in processing this Rule Change Proposal are:



Based on the submissions received, the IMO's draft decision is to implement the Rule Change Proposal in the form outlined in section 6 of this Report.

This Draft Rule Change Report on the Rule Change Proposal has been prepared by the IMO in accordance with clause 2.7.6 of the Market Rules.

Interested parties are invited to provide further submissions in relation to this Draft Rule Change Report. In accordance with the Market Rules timelines, the deadline for submissions is 19 December 2008.

2. THE RULE CHANGE PROPOSAL

2.1. Submission Details

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Date submitted:	<i>11 September 2008</i>
Urgency:	<i>High</i>
Change Proposal title:	Eligible services for Supplementary Reserve Capacity

2.2. Details of the Proposal

The IMO submitted that the Registered Facilities that are permitted to enter the Supplementary Reserve Capacity (SRC) process include those facilities with spare capacity (i.e. capacity that does not hold Capacity Credits) in the current Reserve Capacity cycle but which hold Capacity Credits for future cycles. The IMO posited that this condition is necessary so as to prevent Registered Facilities with Capacity Credits in previous Reserve Capacity cycles from withholding them from the normal Capacity Credit processes so as to activate the SRC process and benefit from much higher prices.

The IMO's proposed amendments also clarify that Market Customers with a Demand Side Program that have failed to satisfy their Reserve Capacity Obligations in accordance with clause 4.8.3(d) cannot participate in the SRC process.

The IMO stated that a regular review of the SRC process against the market objectives was suggested by the SRC Working Group, given the fact that the use of SRC may place a considerable financial burden on the market and that it was intended to be a very infrequent event.

The IMO proposed that clause 4.24.19 be added stipulating that a review must follow each call for tenders of SRC where that review must entail an assessment of the appropriateness of the provisions pertaining to SRC under clause 4.24 and a public consultation process seeking to garner feedback on the outcome of the review.

2.3. *The Proposal and the Wholesale Market Objectives*

The IMO's assessment on how these amendments will allow the Market Rules to better address the market objectives is contained in section 4.1.2 of this Report.

2.4. *Amending Rules proposed by the IMO*

The IMO proposed the following amendments to the Market Rules (~~deleted words~~, added words):

4.24.3. The only eligible sources of supplementary capacity are the following services ("**Eligible Services**"):

- (a) load reduction, that is measures to reduce a consumer's consumption of electricity supplied through the SWIS, but excluding reductions associated with the operation of Registered Facilities (including registered Loads) or reductions provided by a Market Customer with a Demand Side Programme that does not satisfy its Reserve Capacity Obligations for the current Reserve capacity Cycle in accordance with clause 4.8.3(d) at the time the IMO seeks to acquire supplementary capacity; and
- (b) the generation of electricity by generation systems that are not Registered Facilities;
- (c) the generation of electricity by generation systems, or load reductions provided by loads, that are Registered Facilities but only to extent that:
 - (i) the electricity is generated, or the load reduction is provided, by capacity for which the relevant Market Participant does not hold Capacity Credits in the current Reserve Capacity Cycle; and
 - (ii) the electricity is not generated, or the load reduction is not provided, by capacity which has provided Capacity Credits in the current Reserve Capacity Cycle or a previous Reserve Capacity Cycle; and
 - (iii) the electricity is generated or the load reduction is provided, by capacity for which the relevant Market Participant holds Capacity Credits in a subsequent Reserve Capacity Cycle.

4.24.19. Following each call for tenders for supplementary capacity or otherwise acquiring Eligible Services, the IMO must review the Supplementary Reserve Capacity provisions of this section 4.24 of the Market Rules with regard to the Wholesale Market Objectives and must undertake a public consultation process in respect of the outcome of the review.

2.5. *The IMO's Initial Assessment of the Proposal*

The IMO decided to proceed with the proposal on the basis of its preliminary assessment, which indicated that the proposal was consistent with the Wholesale Market Objectives. This preliminary assessment was published in a Rule Change Notice on 12 September 2008.

3. SUBMISSIONS

During the first public submission period the IMO received submissions from Landfill Gas & Power Pty Ltd (LGP), Synergy and Alinta. The details of the submissions received during the submission period and the outcomes from any discussions of the proposal at public forums and workshops are summarised below. The full text of the public submissions is also available on the IMO website.

3.1. *Public Forums and Workshops*

No public forums or workshops were held in relation to this Rule Change. The proposed Rule Change was discussed at the Supplementary Reserve Capacity (SRC) Working Group and the Market Advisory Committee (MAC) meetings.

3.1.1 *Supplementary Reserve Capacity Working Group*

At the SRC Working Group meeting on the 15 September 2008 it was noted that amendments needed to be made to the published rule change proposal entitled 'Eligible Services for SRC' during the preparation of the relevant draft report. The proposed amendment was to include physical equipment installed specifically to provide additional capacity for the purpose of SRC to be an additional source of SRC. It was agreed that the amending rules needed to be changed to allow market participants committing to install equipment to provide additional capacity at Registered Facilities to participate in a Supplementary Capacity Contract.

At the final meeting of the SRC Working Group on 22 September 2008, changes to the amending rules were proposed. In addition, the IMO has identified two other minor changes to improve the drafting of the rules. These changes are as follows (~~deleted words~~, added words):

- 4.24.3. The only eligible sources of supplementary capacity are the following services ("**Eligible Services**"):
- (a) load reduction, that is measures to reduce a consumer's consumption of electricity supplied through the SWIS, but excluding reductions associated with the operation of Registered Facilities (including registered Loads) ~~or~~ and reductions provided by a Market Customer with a Demand Side Programme that does not satisfy its Reserve Capacity Obligations for the current Reserve eCapacity Cycle in accordance with clause 4.8.3(d) at the time the IMO seeks to acquire supplementary capacity;
 - (b) the generation of electricity by generation systems that are not Registered Facilities;
 - (c) the generation of electricity by generation systems, or load reductions provided by loads, that are Registered Facilities but only to extent that the electricity is generated, or the load reduction is provided, by capacity for which the relevant Market Participant, either:
 - (i) does not hold Capacity Credits in the current Reserve Capacity Cycle; and

- (ii) has not held Capacity Credits in the current Reserve Capacity Cycle or a previous Reserve Capacity Cycle; and
- (iii) holds Capacity Credits in a subsequent Reserve Capacity Cycle;
or
- (iv) provides evidence satisfactory to the IMO, prior to a Supplementary Capacity Contract taking effect, that:
 - 1. costs have been incurred to enable the provision of the capacity through the installation of physical equipment; and
 - 2. the capacity is in addition to the sent out capacity of the generation system, or the maximum amount of load that can be curtailed, that existed prior to the installation of the physical equipment.

4.24.19. Following each call for tenders for supplementary capacity or otherwise acquiring Eligible Services, the IMO must review the Supplementary Reserve Capacity provisions of this section 4.24 of the Market Rules with regard to the Wholesale Market Objectives and must undertake a public consultation process in respect of the outcome of the review.

3.1.2 Market Advisory Committee

The MAC was first advised of the proposed rule change at its meeting on 10 September 2008, before it was formally submitted by the IMO. At the meeting, MAC was in general support of the proposal and of the IMO submitting it as a formal Rule Change Proposal.

MAC members were also invited to discuss the proposal at the MAC meeting on 8 October 2008, after the proposal had been published on the IMO website. MAC advised that, in accordance with the SRC Working Group's decision, the amending rules needed to be changed so that physical equipment installed specifically for the purpose of SRC was included as a source of additional capacity. The IMO agreed with the MAC's recommendations and has subsequently amended the proposed rule change to reflect the SRC Working Group's suggestions.

3.2. Submission from LGP

LGP expressed its support for the Rule Change Proposal on the grounds that it permits a generator that has commissioned new capacity, before the date on which the Reserve Capacity obligations commences, to make that capacity available in the event of SRC being required. Further, LGP noted that the proposed change involved safeguards to prevent gaming, where a generator could otherwise cause the need for SRC by withholding its capacity from the intended process and then achieving a higher price by participating in the SRC process.

3.3 Submission from Synergy

Synergy expressed its support for the Rule Change Proposal on the grounds that consideration by the SRC Working Group, of whom Synergy was the Chair, unanimously endorsed the resultant Rule Change as an appropriate means of ensuring reliability through the Reserve Capacity Mechanism whilst maintaining economic efficiency. Additionally, it was noted that the exact wording of this rule change was subject to considerable deliberations within the Working Group to ensure that the risks of Market Participants taking advantage of the SRC process, extracting supernormal profits through subverting the standard Reserve Capacity Cycle, were mitigated.

Synergy supported the IMO's view that the condition of holding capacity credits for future cycles is very necessary in order to prevent Registered Facilities with capacity credits in previous Reserve Capacity cycles from withholding them from the normal capacity credit processes so as to activate the SRC process and benefit from much higher prices.

Synergy stressed that the use of the SRC process has the potential to place a substantial financial burden on Market Customers (retailers) and in turn, on their end-use customers. The original market design contemplated SRC as being a very rare event. Synergy therefore strongly supports Clause 4.26.15, which necessitates a review each year, following any call for SRC, which assesses the appropriateness of the SRC mechanism and seeks to make improvements for any future application of SRC.

In its submission, Synergy perceived the rule change as being urgent due to the imminent commencement of the summer period and the very tight demand/supply balance for capacity. It is Synergy's opinion that it is critical that this rule change be expedited.

3.3 Submission from Alinta

Alinta agreed with the Rule Change Proposal as it strikes an appropriate balance between avoiding the potential for gaming and maximising the availability of SRC providers in the event that SRC is called. However, they noted that the proposed rules may still prevent some service providers from participating that would not have been available for SRC in any case. For example, a generating facility intending to decommission may defer this if they could meet an SRC requirement, potentially at a far lower cost to other sources. Their lack of future accreditation under the proposed rules would prevent this.

Alinta recommended that while the current proposal is a step in the right direction, future developments in this area should consider enticing other potential sources of SRC while still preventing gaming.

Alinta perceived the rule change as increasing the competitive tension involved in providing SRC and therefore would promote achievement of objectives (a) and (d) of the Market Rules. They do not consider the rule change would impede the achievement of any of the other market objectives.

4. THE IMO'S ASSESSMENT AND DECISION

4.1. Assessment

4.1.1. Submissions

All parties responding to the IMO's invitation for submissions expressed support for the Rule Change Proposal albeit with requests for changes to be made to the amending rules by the SRC Working Group and the MAC as outlined in section 3.1.

Alinta suggested that future developments in this area should consider enticing other potential sources of SRC while preventing gaming. The IMO notes that the agreed changes to allow participants committing to installing equipment which specifically provides additional capacity at Registered Facilities will go some way towards addressing this consideration. Additionally, the IMO acknowledges Alinta's point that there may be some examples where the proposed rules may still prevent some service providers from participating that would not have been available for SRC in any case. However, the IMO perceives that there needs to be a balance between the complexity of the market rules and encompassing the majority of situations. The IMO has therefore decided not to provide any additional amendments in its draft amending rules.

4.1.2. The IMO's Assessment

According to clause 2.4.2 of the Market Rules *"the IMO must not make Amending Rules unless it is satisfied that the Market Rules, as proposed to be amended or replaced, are consistent with the Wholesale Market Objectives"*.

The IMO considers that the proposed Amending Rules will have the following impact on how the Market Rules address the Wholesale Market Objectives:

Impact	Wholesale Market Objectives
Allow the Market Rules to better address objective	a
Consistent with objective	b, c, d and e
Inconsistent with objective	-

The IMO's assessment against market objectives (a) and (d) is 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;*

The IMO submits that the proposal supports market objective (a) by ensuring that if SRC is called, sufficient capacity will be available to participate in the process.

The IMO submits that the proposal is consistent with the remaining market objectives.

In accordance with Clause 2.4.3(b) of the Market Rules, in deciding whether or not to make Amending Rules, the IMO must also have regard to the practicality and cost of implementing the amending rules.

The proposed changes do not require any change to the Wholesale Electricity Market Systems operated by the IMO. No other costs have been identified in relation to the implementation of the proposed change.

4.2. IMO's Draft Decision

The IMO's draft decision is to implement the proposed amendments to clauses 4.24.3 and 4.24.15 as proposed by the IMO and amended during the first submission period as result of subsequent recommendations from the SRC Working Group and agreed by the MAC (as discussed in section 3.1) .

The IMO has made its draft decision on the basis that the resulting Amending Rules will allow the Market Rules to better address the Wholesale Market Objectives.

The wording of the relevant Amending Rules is presented in section 6 of this Report.

5. CALL FOR SUBMISSIONS

The IMO invites Market Participants to make submissions on this Draft Rule Change Report and proposed Rule Change. The submission period is 20 Business Days from the publication date of this Report.

Submissions must be delivered to the IMO by close of business on Friday 19 December 2008.

The IMO prefers to receive submissions by email to marketadmin@imowa.com.au using the submission form available on the IMO website:

http://www.imowa.com.au/10_5_1_b_rule_change_proposal.htm

Submissions may also be sent to the IMO by fax or post, addressed to:

Independent Market Operator
Attn: Manager Market Administration
PO Box 7096
Cloisters Square, Perth, WA 6850
Fax: (08) 9254 4399

6. PROPOSED AMENDING RULES

The IMO proposes to implement the following amendments to the Market Rules (added words are underlined and deletions are shown with a ~~strikethrough~~):

- 4.24.3. The only eligible sources of supplementary capacity are the following services ("**Eligible Services**"):
- (a) load reduction, that is measures to reduce a consumer's consumption of electricity supplied through the SWIS, but excluding reductions associated with the operation of Registered Facilities (including registered Loads) ~~or~~ and reductions provided by a Market Customer with a Demand Side Programme that does not satisfy its Reserve Capacity Obligations for the current Reserve ~~e~~Capacity Cycle in accordance with clause 4.8.3(d) at the time the IMO seeks to acquire supplementary capacity;
 - (b) the generation of electricity by generation systems that are not Registered Facilities;
 - (c) the generation of electricity by generation systems, or load reductions provided by loads, that are Registered Facilities but only to extent that the electricity is generated, or the load reduction is provided, by capacity for which the relevant Market Participant, either:
 - (i) does not hold Capacity Credits in the current Reserve Capacity Cycle; and
 - (ii) has not held Capacity Credits in the current Reserve Capacity Cycle or a previous Reserve Capacity Cycle; and
 - (iv) holds Capacity Credits in a subsequent Reserve Capacity Cycle;
or
 - (iv) provides evidence satisfactory to the IMO, prior to a Supplementary Capacity Contract taking effect, that:
 - 1. costs have been incurred to enable the provision of the capacity through the installation of physical equipment; and
 - 2. the capacity is in addition to the sent out capacity of the generation system, or the maximum amount of load that can be curtailed, that existed prior to the installation of the physical equipment.
- 4.24.19. Following each call for tenders for supplementary capacity or otherwise acquiring Eligible Services, the IMO must review the Supplementary Reserve Capacity provisions of this section 4.24 of the Market Rules with regard to the Wholesale Market Objectives and must undertake a public consultation process in respect of the outcome of the review.

7. GENERAL INFORMATION ABOUT RULE CHANGE PROPOSALS

Clause 2.5.1 of the Wholesale Electricity Market Rules (Market Rules) provides that any person (including the Independent Market Operator) may make a Rule Change Proposal by completing a Rule Change Proposal Form and submitting this to the Independent Market Operator (IMO).

In order for the proposal to be progressed, the change proposal must explain how it will enable the Market Rules to better contribute to the achievement of the Wholesale Market Objectives. The market objectives are:

- (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
- (e) to encourage the taking of measures to manage the amount of electricity used and when it is used

A Rule Change Proposal can be processed using a Standard Rule Change Process or a Fast Track Rule Change Process. The standard process involves a combined 10 weeks public submission period. Under the shorter fast track process the IMO consults with Rule Participants who either advise the IMO that they wish to be consulted or the IMO considers have an interest in the change.