



22 April 2013

Ms Reena Kwong
Australian Energy Market Operator
PO Box 7326
Baulkham Hills BC NSW 2153

Submitted via: www.aemo.com.au

Dear Ms Kwong,

Value of Customer Reliability

Alinta Energy welcomes the opportunity to make a submission in response to the Australian Energy Market Operator's (AEMO) issues paper entitled *Value of Customer Reliability*.

Alinta Energy is an active investor in the energy retail, wholesale and generation markets across Australia. Alinta Energy has over 2500MW of generation facilities in Australia (and New Zealand), and maintains approximately 700,000 retail customers across Australia.

Energy reliability is essential to underpinning Australia's future economic growth and prosperity. As such, achieving an appropriate balance between community expectations and the level of infrastructure investment required to meet this expectation is a challenging task. Recent debates regarding the cost of electricity networks demonstrate this.

In this regard, the issues paper provides a timely opportunity to review the current methodology for determining the value of customer reliability (VCR).

Shortcomings and potential improvements to the development of VCR

At present, VCR data is segmented on a regional basis and a sector specific basis for residential, commercial, industrial and agricultural energy users. The VCR data is not segmented between different types of energy users within each region, providing little insight into potentially diverse regional-sector specific needs.

For example, it is likely that an "Urban Commercial" energy user will have a significantly different VCR to a "Rural Commercial" energy user, due to a range of potential factors; for instance the potential for privately owned back up generation.

Assuming it is not cost prohibitive, Alinta Energy suggests that VCR's be calculated on a segmented basis across and within regions, including market indicators such as urban, rural and city users. The benefit of this approach is a more refined depiction of the market place.

Approaches to deriving an improved VCR methodology

Currently, the VCR survey approach focuses on estimating consumers' out of pocket expenses that result from a loss of energy reliability. This approach tends to understate the real value of VCR by

excluding non-financial losses. These non-financial losses include economic costs and inter-linkages between sectors of the economy.

For this reason, Alinta Energy is supportive of incorporating contingent valuation survey methodologies within the current existing survey procedure. This additional feature would only be a minor change to the existing practise, and would provide an opportunity for customers to place a financial value on their willingness to pay to avoid a potential power interruption, and their willingness to accept a potential interruption.

Alinta Energy appreciates that in order to develop a practical survey design, which gathers meaningful results, a combination of the different proposed methods may be appropriate. A combination of methods would also resolve any theoretical limitations within the contingent valuation methodology.

Nonetheless, inclusion of the contingent valuation approach is well suited to take into account non-financial customer losses, previously unmeasured, and will at a minimum provide an accurate expectation of the future value of reliability of supply across all sectors.

Relevance to wholesale energy market and market price cap

Alinta Energy notes that VCR can play an important role in transmission planning by expressing the willingness to pay for additional transmission investment. By contrast the Market Price Cap (MPC) limits the revenue that can be recovered by generators to a level below this.

The Reliability Panel has previously used the VCR as a comparator in determining the MPC as it informs a consumer's willingness to pay¹. For instance, the existing MPC of \$12 900 MWh (indexed to the consumer price index) is generally consistent with the previously determined VCR for the residential sector of \$13 250 MWh.

However, this ignores the overall value of the VCR by excluding industrial, commercial and agricultural sectors across all states. Alinta Energy notes the AEMO assessment of VCR provides the following breakdown by region, providing an average of \$47.68 per KWh unweighted.

VCR by Region					
VCR	NSW	QLD	SA	TAS	VIC
2010 KWh	41.53	44.31	44.3	50.97	57.29

This implies a national VCR of approximately \$47,680 MWh, and whilst clearly only a simple average, this is indicative of the current inconsistency between the VCR and the MPC.

Failings in MPC not currently reflected in VCR

The MPC is used to provide sufficient incentive for peaking generation investment, which in turn ensures that the reliability standard will be met. This marginal generation has to be adequately profitable, through recovery of fixed costs, at the known reliability standard and MPC.

Capital and operating costs for this new entrant peaking generation should be recoverable purely in the wholesale market, within the limited amount of running hours in which an unserved energy event is occurring. These running hours are limited in light of the fact that this specific generator would be the last to be dispatched.

¹ AEMC (2010) , Reliability Standard and Reliability Settings Review, Reliability Panel, pg xi.

Generation and transmission

Presently, Alinta Energy is of the view that inconsistencies between the MPC and VCR need to be reconsidered. Having two divergent values, which at first glance appear to favour transmission networks, is an inefficient outcome, and undervalues investment in generation.

Notably, transmission investment is paid for by consumers and there is little opportunity for consumers to respond to transmission price signals once built. In direct contrast, new generation investment is generally funded by private enterprises that only recover their investment when the service is being used. For this reason, it is uneconomic to mandate transmission solutions, over generation solutions.

Furthermore, generation solutions provided at the local level, are likely to be far more economic and market responsive than high voltage transmission network upgrades. These generation solutions also have the added benefit of being able to be built in smaller increments in order to satisfy market needs. This is particularly relevant as smaller generation solutions provide additional flexibility in an evolving market.

In terms of achieving an appropriate balance between reliability and cost, generation solutions meet allocative and price efficiency criteria considered essential under any well functioning VCR methodology.

This suggest a closer alignment of the VCR and MPC may be needed to provide assurance that sufficient incentives exist for generation to be built to satisfy reliability standards and customer expectations of reliability at least cost.

Conclusion

Apart from these considerations, Alinta Energy broadly welcomes the issues paper and appreciates the work of AEMO.

Should you have any queries in relation to this submission, please do not hesitate to contact me on, telephone, (02) 9372 2633, or Anders Sangkuhl on (02) 9375 0962.

Yours sincerely,



Jamie Lowe
Manager, Market Regulation