

15 November 2021



Oliver Derum
Principal Analyst
Australian Energy Market Operator

Submitted electronically to isp@aemo.com.au

Dear Oliver,

Updates to benefits calculation in the Inputs, Assumptions and Scenarios Report

The Public Interest Advocacy Centre (PIAC) is leading social justice law and policy centre. Established in 1982, we are an independent, non-profit organisation that works with people and communities who are marginalised and facing disadvantage. PIAC builds a fairer, stronger society by helping to change laws, policies and practices that cause injustice and inequality. The Energy and Water Consumers' Advocacy Program (EWCAP) represents the interests of low-income and other residential consumers of electricity, gas and water in New South Wales. The program develops policy and advocates in the interests of low-income and other residential consumers in the NSW energy and water markets

PIAC welcomes the opportunity to respond to the Australian Energy Market Operator's (AEMO) consultation on calculating competition benefits in Integrated System Plan (ISP) analysis.

PIAC appreciates AEMO's consultation on including competition benefits as part of the range of benefits claimed in the Integrated System Plan (ISP) cost benefit analysis (CBA). However, PIAC considers competition benefits measured using the approach proposed by EY are too uncertain to include in ISP modelling and should remain excluded. PIAC also considers, given the draft 2022 ISP is due to be published in December, it is too late in the 2022 ISP development process for this discussion of competition benefits. We discuss our reasons for opposing including competition benefits using the EY method below.

A simplified approach is not appropriate

AEMO acknowledges the complexity of measuring competition benefits for ISP projects in its recent ISP Methodology:

Quantification of competition benefits is a challenging task even when considering a single investment. Including competition benefits throughout the consideration of alternative Development Paths on a whole-of-system plan would not be possible, nor would the benefits be expected to be material relative to project costs.¹

We note AEMO is considering a simplified approach to measuring competition benefits due to this complexity. While it is possible some level of competition benefits exists, their predicted

¹ AEMO, 2021. *ISP Methodology*. <https://aemo.com.au/-/media/files/major-publications/isp/2021/2021-isp-methodology.pdf?la=en>, 74.

timing and magnitude will be heavily influenced by the modelling input assumptions. Simplifying assumptions means the error bars surrounding the estimated benefits would be too large to be of any real use and certainly not fit to justify large network expenditure.

Modelling assumptions need more rigour

PIAC strongly supports the critique of the modelling assumptions provided by Shell Energy in its submission to this consultation. We highlight a number of key points which should dissuade AEMO from using the EY approach.

The current scale and rate of change in the NEM makes it increasingly challenging to make valuable assumptions regarding potential generator bidding strategies over the modelling period. Bidding outcomes post the recent change to 5-minute settlement are in flux with the impact of this change still to be fully understood by participants. In the medium term, a capacity mechanism of some description, as recommended by the Energy Security Board in its Post-2025 market design work, would majorly change the economics of generation and generators' bidding strategies. The simplified models EY has proposed could be obsolete within as little as 12-24 months.

The existing assumptions around which participants are strategic bidders and to what extent are contentious and not necessarily accurate and robust. There is no defined selection or analysis criteria for EY's choice of strategic bidders or the level of strategic bidding. As such, we do not consider it reasonable to use this generically for the ISP. There can be strategic players in each market at different times and strategic bidding is not guaranteed to occur at any time. We recommend AEMO undertake additional consultation and analysis regarding input assumptions prior to commencement of any modelling of competition benefits. The choice of strategic participants and the level of strategic choice allowed is the most critical and contentious part of competition benefits modelling and must be subject to rigorous and transparent consultation.

The assumption demand is materially elastic in response to falls in electricity prices is unlikely. People (and businesses) generally reduce energy costs by making investments in resources like solar PV and energy efficiency. These investments have long lives and, while they are operating, would likely make energy demand fairly inelastic to prices. Further, the study EY references to support its assumptions on demand elasticity focusses on responses to increases in prices, not decreases, and its conclusions should not be applied in the case of falling wholesale prices.

The long-term benefits of a reduction in wholesale prices are not clear. If a Candidate Development Path (CDP) reduces wholesale prices materially this is likely to disincentivise generation investment, which may in turn push wholesale prices back up.

Risks of over-stating benefits

PIAC is deeply concerned these highly uncertain competition benefits will be used to justify network projects that may otherwise not produce a net benefit. While any project published in the ISP would still be subject to a comprehensive cost-benefit analysis, the presence of the project in the ISP allows for the Regulatory Investment Test for Transmission (RIT-T) process to be shortened. In completing any subsequent RIT-T process the proponent is also allowed to utilise benefit modelling outcomes from the ISP. The costs of transmission projects are definite and passed onto consumers but the benefits to consumers only accrue in theory over several years. Consumers face certain costs, but uncertain benefits.

The decision to include competition benefits or not, based on the proposed methodology, also appears to create an asymmetry. If preliminary modelling suggests that a material competition benefit exists, it can and would be included. However, if modelling were to show that there was

a net market disbenefit from the inclusion of competition benefits, there does not appear to be an obligation to include it. PIAC considers disbenefit could occur where the commissioning of additional transmission capacity leads to early exit of existing capacity or a change in generation development plans. This kind of optionality undermines the regulatory process surrounding transmission investment. AEMO should clarify whether it proposes to assess material competition benefits for certain CDPs only if there are positive benefits or also if there are negative benefits.

PIAC would welcome the opportunity discuss these matters further with AEMO.

Yours sincerely

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