

24 August 2023

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Your Ref: ERC0366

Dear Ms Dartnell-Moore,

### **Extension of the application of the IRM to the RRO**

The Public Interest Advocacy Centre (PIAC) welcomes the opportunity to respond to the draft rule determination for the National Electricity Amendment (Extension of the Application of the IRM to the RRO) Rule (the Rule).

#### **PIAC does not support the Rule.**

It has not been established that the rise of tail risks during the period to 30 June 2028 warrants this short-term measure. An interim reliability measure (IRM) substantially below the level of the reliability standard is, in any case, a poor measure to manage a problem of that nature.

It is too imprecise, adds no market signal to investors that does not already exist, and provides no incentive to increase the net capacity of the NEM in response to anticipated shortfalls.

There are other ways to manage the possibility of outages in the period. Many of these are already in place or anticipated:

- raising the market settings (anticipated);
- the Capacity Investment Scheme (CIS) (existing);
- the orderly exit framework (existing);
- extending the application of the Interim Reliability Reserve (IRR) (anticipated); and
- jurisdictional measures such as the NSW EI Roadmap (existing).

There are also options such as boosting storage and utilisation of demand response, and supercharging energy efficiency improvements. These are all occurring in different ways at the jurisdictional level, but could be further increased or accelerated.

As has been widely noted, including by the AEMC's Reliability Panel, the IRM does not reflect consumers' preferences with regard to reliability.

Contrary to the AEMC's contention, the Rule does not support certainty for market participants. The creation of a second unserved energy standard undermines the governance structures of the reliability regime and the primacy of the Reliability Panel and the market settings. It overstates the likelihood of material outages by adding expected shortfalls that lie between the two standards, shortfalls that are relevant for some elements of the regulatory system and not for others.

The AEMC's note in the draft rule determination that the IRM may continue to be applied after 30 June 2028, despite the fact the Reliability Panel's new form of the reliability standard is expected to be introduced at that time, further increases the uncertainty participants face. Notably, market participants who made submissions to the original consultation overwhelmingly opposed the extension of the application of the IRM to the RRO, a number of them on the grounds that it creates uncertainty.

The design of the RRO is deeply flawed. There is no reason to believe it has or will increase energy capacity in the NEM. Among more detailed problems outlined in submissions to the 2023 Review of the RRO (such as those from Shell, Tom Geiser, and South Australian Water), it relies on mandated short term financial products that are starkly at odds with any energy investment timeframe. It operates at a degree of remove from the generators capable of increasing capacity in the system. It is not salvageable and far from extending the application of the IRM to the RRO, the RRO itself should be abandoned.

### **The AEMC's consultation process has not been adequate.**

None of the arguments above are new to the Commission. They all appear in some form in the submissions to the two consultation processes this year which are pertinent to this determination: the Review of the RRO and the Review of the IRM. Concerns about the functioning of the RRO are relevant to the question of whether application of the IRM to the RRO should be extended. The AEMC should have engaged with the concerns raised in that process in this draft rule determination.

In both of those consultations the majority of respondents opposed the continuation of the RRO or IRM. This is more pronounced if responses from regulators are not included.

As the AEMC has acknowledged, "of the eight [submissions on the draft recommendation to extend the application of the IRM to the RRO], two supported the draft recommendation, five did not support and one was neutral on the need for the IRM."

In the case of the Review of the RRO, nine of the fifteen submissions opposed the continuation of the RRO. The depth of the opposition is strengthened when it is noted that the overall effectiveness or validity of the RRO were out of scope.

Aside from opposition to the scheme in total, the themes emerging from the two consultations are relatively coherent. Stakeholders contend the scheme is not fit for purpose, did little if anything to contribute to reliability, and is not in the interests of consumers or market participants.

While the AEMC can make a determination opposed by a majority of respondents, meaningful engagement requires them to respond substantively to the concerns raised. That has not occurred here.

The following is a table listing the concerns raised by stakeholders opposed to the extension of application of the IRM to the RRO and to the RRO itself.

| <b>Concern</b>   | <b>Stakeholder</b>  | <b>AEMC response</b>   |
|--|---|--|
| The recommendation to extend the application of the IRM does not rest on any economic modelling.   | Alinta Energy   | No new modelling has been provided.  |
| The recommendation to extend the application of the IRM is inconsistent with the Reliability Panel's (RP) findings.  | Alinta Energy   | The AEMC disingenuously implies that the RP's concern about the rise of tail risks extends to supporting this (or any) interim measure to manage these risks.  |
| The IRM does not reflect consumer willingness to pay for reliability.  | Energy Australia, Shell, Energy Users Association Australia, PIAC | The AEMC notes that the IRM has limited application, compared to the reliability standard. This does not resolve this concern satisfactorily.  |
| Extending the application of the IRM will not drive new capacity.  | Shell   | Not responded to.  |
| The RRO has been superseded by developments such as the likely raises to the market settings, the CIS, the orderly exit framework, and the possible extension of the application of the IRR. | Origin, Energy Australia, Tom Geiser, PIAC                        | Not responded to.  |
| Extending the application of the IRM creates more uncertainty for market participants.   | AEC, Alinta Energy  | The AEMC claims that '[e]xtending the IRM supports certainty in the reliability framework'. No real basis is provided for this claim, and none of the specific concerns relating to certainty raised in the two consultations are engaged with. The paragraph under the heading quoted provides unrelated justifications for the determinations. |
| The RRO is complex and costly.   | AEC, Engie, PIAC  | The AEMC has responded to the concern about the risk of increased costs to consumers. It claims that the extension of the application to the IRM is warranted despite the increased cost and that the costs resulting from the extension are likely to be low.   |

|  |                               |   |
|--|-------------------------------|---|
| The RRO does not contribute to reliability as it does not incentivise new capacity.  | AFMA, Engie, Tom Geiser, PIAC | Not responded to.   |
| The RRO incentivises consumers to not exercise demand response and so exacerbates demand volumes during forecast shortfall periods.  | South Australian Water        | Not responded to.   |
| The RRO has a design flaw: retailers do not want to sign up new customers unless they can be assured the AER will permit them to adjust their net contract positions (NCP), but retailers cannot be assured the AER will permit them to adjust their NCPs unless they have already signed up the new customer. | Shell                         | Not responded to.   |
| The RRO increases costs for consumers by rendering buyers of energy contracts captive during the book build.   | Tom Geiser                    | Not responded to. (Concerns about costs to consumers are responded to, but not via this mechanism.) |

The AEMC has not responded to many of the concerns raised. Of the issues it has responded to, the reasoning for rejecting the concern is inadequate.

In addition to the AEMC positions outlined above, three further positions the AEMC takes do not address or overcome the concerns previously raised by stakeholders.

- The AEMC cites AEMO’s position that the IRM is an effective investor signal. But this is not compelling justification. The market signals rest on the information contained in the ESOO. The IRM and RRO add no further information to market participants. Further, the obligation of the RRO does not fall on generators and the timeframe of the obligations is not aligned with investment timeframes.
- The AEMC claims that the IRM is consistent across the NEM and preferable to jurisdictional approaches. This is a straw man. The alternative measures listed in the table as developments in the NEM that render the IRM and RRO redundant – the market settings, CIS, orderly exit framework, and IRR – are all NEM-wide. Any jurisdictional approaches occur in addition to these NEM-wide measures.
- The AEMC acknowledges that while the market expected the IRM would be in place until 30 June 2025, the intention was always actually to keep it in place until ‘enduring market design’ is implemented. It seems clear that the AEMC is acknowledging that extending the IRM is the unexpected outcome,<sup>1</sup> and it is not clear how extending it to an ambiguously

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<sup>1</sup> To be clear, it is very reasonable for market participants to have believed until now that the IRM would cease to be used after 30 June 2025. Statements such as the following, taken from AEMO’s Electricity Statement of Opportunities (ESO), 2022, p.6, are not ambiguous:

“The Interim Reliability Measure (IRM) was introduced to reduce the risk of load shedding across the NEM, providing a trigger for the Retailer Reliability Obligation (RRO) of 0.0006% of energy demanded in a region in any year. It applies until 30 June 2025.”

defined endpoint reduces uncertainty. This is exacerbated by the draft determination introducing the possibility that the application of the IRM may be extended beyond 30 June 2028, by which time the non-interim response to the rise of tail-risks, the new form of the reliability standard, is expected to be introduced.

We agree with Shell and the Energy Users Association of Australia, who both note in their submissions that it appears that the draft recommendation did not reflect consumers' views on the value of reliability and instead focuses more on an undefined political value of reliability.

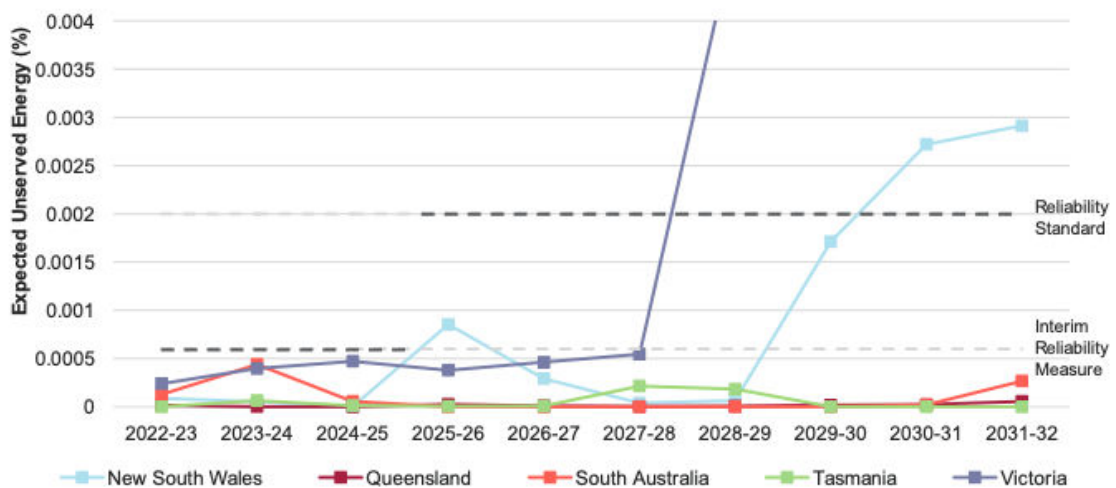
In PIAC's view, the AEMC is clearly failing to reflect the preferences or interests of consumers in recommending continuation of the IRM. It is also engaging in consultations which do not uphold key aspects of good engagement.

**There are potentially material impacts of the determination being baked in before the consultation period has been completed.**

There are material consequences in leaving open the possibility of the IRM being extended beyond the official expiry date of 30 June 2025.

In the 2022 Electricity Statement of Opportunities, the IRM was included alongside the reliability standard. It was made clear in the text throughout that the IRM's relevance was limited in time. However, in graphs depicting expected shortfalls, such as that on page 9, and recreated below, the significance of the IRM beyond June 2025 was more ambiguous. (Indeed, the graph suggests that the reliability standard is not significant before 30 June 2025, which is not the case.)

**Figure 2 Expected unserved energy, ESOO Central outlook with anticipated and actionable developments, 2022-23 to 2031-32 (%)**



**The reliability gaps forecast in the next five years are despite new committed investments connecting**

It is entirely possible that inclusion of the IRM beyond the official expiry date of 30 June 2025 in documents such as the ESOO will give the impression of expected outages. By contrast,

taking the established standard for the period would result in no expected outage. That is, the IRM may have material impacts even if no official decision to extend its application has been made (which is currently the case).

The public and media narrative resulting from the release of the ESOO is often framed in relation to 'expected blackouts' or generation shortfall, and this narrative has potential implications and impacts on Government decisions; for example, the imminent decision by the NSW Government on whether or not to keep Eraring open beyond its anticipated closure date at great expense. This decision is materially predicated on potential 'generation shortfalls' that are almost wholly dependent upon the application of the IRM.

We welcome the opportunity to meet with the AEMC and other stakeholders to discuss these issues in more depth. Please contact me at [mlynch@piac.asn.au](mailto:mlynch@piac.asn.au) regarding any further follow up.

Yours sincerely,

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