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2 February 2024

To: Energy Ministers
RE: Orderly Exit Management Framework Consultation

Dear Energy Ministers of NEM Jurisdictions,

Thank you for the opportunity for the Institute for Energy Economics and Financial Analysis (IEEFA) to provide input into the Orderly Exit Management Framework[1] consultation. IEEFA is an energy finance think tank that examines issues related to energy markets, trends, and policies. The Institute's mission is to accelerate the transition to a diverse, sustainable and profitable energy economy.

IEEFA's understanding is that coal power stations need to come out of the system faster than has been planned, in order to meet emissions reduction goals. The Australian Energy Market Operator (AEMO)'s Draft 2024 Integrated System Plan (ISP) forecasts coal power stations will exit two to three times faster than their announced dates, which would be in line with a 1.8-degree trajectory.[2] To keep in line with 1.5 degrees would require even faster coal exits.

Governments and the energy industry need to focus on building renewables and storage as quickly as possible to replace coal power plants, while also encouraging greater use of cost-effective options to reduce or shift demand to reduce the need for power supply capacity. Once enough renewables and storage are built to ensure reliability, coal plants should close as soon as possible.

We believe there is merit in exploring options to ensure reliability as coal exits and to help deliver an orderly transition. We outlined various such mechanisms in a paper *There's a Better Way To Manage Coal Closures Than Paying To Delay Them*.[3] In particular, developing additional system reserves could be a good option for the NEM to explore further at this point in time, as well as financial bond mechanisms to penalise owners of ageing power stations if they do not adhere to minimum reliability performance requirements or elect to close without providing adequate notice.

However, the implementation of an OEMF or any other method for propping up the ongoing operation of a coal generator is subject to considerable pitfalls and risks that make it undesirable and ideally such a mechanism should be avoided.

If an OEMF type mechanism is implemented, any such mechanism needs to examine all other options before subsidising coal- or gas-fired power stations to stay open, given the urgency of emissions reduction. It needs to make sure that any payment to emissions intensive generators does not incentivise levels of generation beyond what is absolutely necessary to ensure power reliability is maintained at satisfactory levels. It also needs to

[1] NSW Government Office of Energy and Climate Change. Orderly Exit Management Framework Consultation Paper. December 2023.
[2] AEMO. Draft 2024 Integrated System Plan. December 2023.
[3] IEEFA. There's a Better Way To Manage Coal Closures Than Paying To Delay Them. September 2021.

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make every effort to reduce costs to consumers, and keep any risk with the entity that is facing the risk and can manage the risk, rather than transferring risk to consumers. In this submission we have outlined a potential structure for the commercial component that could address these objectives. However, we acknowledge that the potential structure we have outlined, and all similar structures have the potential for significant flaws and are best avoided.

In our submission we provide IEEFA's detailed view on various sections of the consultation paper. We also summarise our high-level comments on the OEMF below.

Please get in touch in case of any questions.

Kind regards,

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Tristan Edis – Guest Contributor, IEEFA

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Overall comments on the framework

The implementation of an OEMF or any other method for propping up the ongoing operation of an ageing, emissions intensive generator is subject to considerable pitfalls and risks that make it undesirable and ideally such a mechanism should be avoided.

- The OEMF involves payments to keep an ageing emissions intensive generator operating beyond its expected closure date. This would likely have significant cost and emissions implications which make it undesirable. It could also lead to market distortion and disincentivise investment in new renewables and storage projects. We outlined these risks in a paper *There's a Better Way To Manage Coal Closures Than Paying To Delay Them*.[4] Due to these risks, IEEFA believes that an OEMF type arrangement should therefore ideally be avoided.
- It is true that the NEM is encountering a range of lags and delays in bringing on new power supply at present. However, given negotiations with Origin Energy over the exit of Eraring Power Station are already in train and the OEMF will not apply to this generator, the earliest the OEM framework is likely to be called upon is 2027. This three-year lead time provides time for Governments and industry to progress an array of measures that should build-up a buffer to allow us to capably manage the exit of another major generator without threatening reliability. In addition, by that time the COVID-related supply chain constraints we have been encountering recently will have likely subsided.
- We suspect that rather than propping up another coal generator (beyond Yallourn and Loy Yang A which already have exit management agreements and potentially Eraring in the near future), governments would be better served using a competitive auction process to build upon the RERT to create a larger reserve of demand reduction and supply options capable of being deployed within a range of timeframes stretching out to potentially as long as two or three years. This would provide a level of reliability insurance that is likely to be far better suited to our emerging future electricity system where we need resources that can respond far more flexibly and reliably than an old coal generator on the verge of retirement.
- Ownership of a very large generator of a size that could put reliability at serious risk if it prematurely exits should come with significant obligations and penalties for failing to support reliability. As we outlined in our paper, *There's a Better Way To Manage Coal Closures Than Paying To Delay Them,*[5] operators of large generating units should be required to provide financial bonds to the government which are ceded in the event a generating unit fails to achieve minimum reliability performance requirements or elects to close without providing adequate notice.

[4] IEEFA. There's a Better Way To Manage Coal Closures Than Paying To Delay Them. September 2021.
[5] IEEFA. There's a Better Way To Manage Coal Closures Than Paying To Delay Them. September 2021.

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In the case that the OEMF or another similar mechanism is implemented, in which the government enters into financial arrangements with exiting, high emissions generators, IEEFA has the below comments on this kind of mechanism.

- Any "system needs shortfall" assessment should be based on the reliability standard rather than the interim reliability measure (IRM). The IRM does not reflect consumer willingness to pay according to Reliability Panel Modelling.
- The OEMF needs to ensure that new renewables investment or build is not deterred and delayed by keeping coal or gas generators operating for longer than reliability needs dictate. Once any system shortfall gap has been closed by the construction of new supply or reductions in demand the emissions intensive generator should cease operation. Any commercial arrangement to subsidise emissions intensive generators to stay open should ensure this occurs through explicit provisions within their contract terms requiring plant closure once the shortfall has been bridged. Governments should specify clearly and publicly the level of the reliability shortfall that necessitates the ongoing operation of each coal unit subject to the agreement and what alternative capacity is necessary to bridge that shortfall. As new supply (or demand reduction) capacity is committed to construction government should publicly report on its likely impact on reducing the projected shortfall over time and therefore when the coal unit could be withdrawn from service. It should also update the shortfall assessment as new capacity is commissioned to show the actual remaining shortfall gap to be bridged.
- The OEMF needs to limit the incentive for the generator in the voluntary or mandatory scheme to generate power beyond what is necessary for it to be available to provide capacity during periods where there is a significant risk of insufficient power supply. This will be important not just to reduce emissions but also to avoid undermining the financial viability of other generators that are likely to be important to maintaining reliable supply. Keeping coal generators operating when they would have exited due to financial dynamics, is likely to push financial problems from the otherwise closing coal generator onto another, while also increasing curtailment of zero emission and lower emission plant that can more easily flex their output.
- The goal of an exit contract should be to incentivise the contracted generator to be available to deliver capacity at times when supply shortfalls are likely (if required) while discouraging output at all other times in order to contain emissions and avoid economic distortions. There are an array of options for how this might be done which will need to involve providing payments to the generator which are not tied to how many megawatt-hours they actually generate but only how many megawatts they offer for dispatch (and duly deliver if AEMO seeks to dispatch them) during times deemed as being at risk of supply shortfalls. Ideally the generator should be required to mothball the plant outside of the winter and summer high demand periods and also strongly encouraged to curtail output as much as possible during negative price events while still being capable of making the necessary capacity available for the afternoon and evening peak demand periods. We have provided one example for how the payments could potentially be structured to achieve this desired outcome,

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but concede that all payment structures have potential for significant flaws. It is not possible to design a perfect contract given the significant complexities involved in the engineering and economics of a coal generator and the fact that government is at a considerable information disadvantage relative to the plant operator, even with the best audit and due diligence advice and information processes.

- IEEFA agrees that a search for alternative solutions should be done before entering a financial arrangement with a coal or gas generator to keep them operating for longer than expected. However, as pointed out above, we would suggest that if the government is concerned about the risk of reliability shortfalls from earlier closure of large generators it should begin a process to establish a larger buffer of capacity in reserve (beyond what is currently provided by the RERT) in advance of being informed about a generator closure being brought forward next coal closure. Emission criteria will be needed when assessing alternative solutions, and the search for alternative solutions should include demand side opportunities and Distributed Energy Resources. We would also suggest that the government could instruct AEMO Services to accelerate the process of awarding of LTESAs to new capacity. AEMO Services has indicated it has had auction rounds where it has had a plentiful number of projects to choose from. While accelerating the awarding of contracts will sacrifice a degree of competitive tension, it comes at the benefit of avoiding all the pitfalls and weaknesses associated with a completely non-competitive process to delay a coal generator from closing earlier than preferred.
- Public consultation should occur at various points in the OEMF. This could be after AEMO has completed the options assessment, and once the cost and information about the commercial arrangement with the generator is available. There should be a framework for consumer challenge of the decision to enter into a contract with an emissions intensive generator.

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Detailed comments on aspects of the framework

IEEFA has outlined our overall comment on the OEMF earlier in this submission: the OEMF or similar mechanisms which prop open an emissions intensive power station should be avoided due to the significant risks and pitfalls involved. However, if the OEMF is implemented in some form, we have the following comments on the framework.

OEMF design principles

The design principles laid out address important goals such as minimising cost to electricity consumers and minimising market distortion.

However, one key design principle that is missing is reducing emissions as soon as possible and reaching government emissions reduction and renewable energy targets. With emissions being included in the National Electricity Objective it is important to ensure various schemes in the National Energy Market (NEM) are in line with that.

The OEM Framework gateway process: Prescribed Information

3. Are there concerns with requiring the Prescribed Information to be provided when the OEM Generator notifies of a change to its closure date (or applies to the AER for an exemption from the notice of closure requirements)? If yes, please provide details.

None from IEEFA's perspective. However, IEEFA notes that the Prescribed Information could be required to be provided by all coal generators – potentially as a requirement of their operating licences. This information would be helpful for the state governments and AEMO in planning the energy system.

The OEM Framework gateway process: System Needs Assessment

Within the gateway process, a system needs assessment is proposed to be undertaken to determine if there is a "system needs shortfall" and the nature of that shortfall.

IEEFA recommends an ongoing system needs assessment be published publicly, to act as a kind of monitor on how close the relevant jurisdictions are in fulfilling the system needs shortfall. Then as soon as it is filled the coal generator can stop operating. This would provide more transparency to the market around coal exit timings, and therefore provide more certainty to investors in new energy infrastructure.

In IEEFA's view, this should be based on the reliability standard rather than the interim reliability measure (IRM), because the reliability standard is the accepted standard for the NEM. The IRM has recently been extended in its application to the Retailer Reliability Obligation (RRO) and the Interim Reliability Reserve (IRR). However, the Reliability Panel found that the IRM does not reflect consumer willingness to pay: "The Panel's analysis indicates the IRM, at 0.0006% expected USE, is significantly tighter than a level of reliability consistent with consumer willingness to pay for reliability. The Panel, therefore, does not consider the IRM is a suitable level for the NEM reliability standard."[6]

Furthermore, on reviewing the stakeholder submissions on the Australian Energy Market Commission (AEMC)'s draft recommendation to extend the application of the IRM to the

[6] Reliability Panel AEMC. Final Report 2022 Review of the Reliability Standard and Settings. 1 September 2022. Page 59.

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RRO to 2028, IEEFA finds there was not broad support for the extension of the application of the IRM to the RRO.[7,8] EnergyAustralia considered that "extending the interim reliability measure (IRM) out to June 2028 would not be in the long-term interests of consumers"[9]; Alinta stated that " the level of 0.002% expected unserved energy (USE) remains appropriate"[10]; while the Australian Energy Council (AEC) "remains unconvinced that the IRM has led to any benefits".[11]

The AEMC points out in the draft rule determination that "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."[12]

The IRM should therefore not be used when making decisions around energy supply for the purposes of the OEMF.

Search for alternative solutions

IEEFA agrees that a search for alternative solutions should be undertaken before subsidising coal or gas generators. Indeed, as stated earlier, we would suggest that government should aim to tender over the next few years for a capacity reserve capable of ensuring reliability in the event of a premature coal exit (if the existing RERT is considered inadequate).

The only reason that government should theoretically need to use the OEMF is because the notice period for a brought forward generator closure is too short to allow for the market to build alternative capacity in time to cover for its exit. The problem at its core is time lags in building new capacity being shorter than the closure notice period. If the government waits until they are informed of a generator closure being brought forward before looking for alternatives, they have set themselves up for failure by ceding valuable time. Once the government establishes an OEMF which guarantees that it will cover a generator's costs plus an additional margin, they will create a temptation for an owner of a large generator facing challenging financial conditions to try to take the government and market by surprise by announcing a closure within a time period they expect will be inadequate for the market or government to cover for the loss of capacity. The only way to counter this time lag problem is to start the process of building up a reserve of rapidly deployable capacity in advance of being taken by surprise of an early coal or gas plant closure. Such a reserve could be composed of capacity with timeframes to deploy that should match the kind of timeframes that the government believes it needs to cover the risk of early generator closure. That should not necessarily mean the kind of very short time frames that the RERT has traditionally targeted and might stretch to as long as two years and maybe three years (beyond this point it should be possible for market participants to respond).

[7] AEMC. Review of the Interim Reliability Measure. Accessed 18 August 2023.
[8] AEMC. Draft Report. Review of the Interim Reliability Measure. 9 March 2023.
[9] EnergyAustralia. Submission to Review of the Interim Reliability Measure – Draft Report. 13 April 2023.
[10] Alinta Energy. Submission – Review of the interim reliability measure. 13 April 2023.
[11] AEC. Submission – AEMC Review of the Interim Reliability Measure: Draft Report. 13 April 2023.
[12] AEMC. Draft Rule Determination National Electricity Amendment (Extension of the IRM to the RRO) Rule. 13 July 2023. Page i.

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Also, emissions should be a part of the evaluation criteria for selecting alternative solutions given how far behind we are in meeting the Paris targets. Moreover, demand-side options and distributed energy resources should be considered in the alternative solutions suite as they have low costs and low emissions.

AEMO's advice on alternative solutions should be completed and published in all situations – including if a Notice for Mandatory Operation is issued, and also if a Voluntary Negotiated Agreement is reached. This enables transparency for the market and provides clarity for consumers on why they may find themselves subsidising legacy coal and gas generators rather than zero emissions solutions.

In the search for alternative solutions, the government should approach the market. A public consultation process should also be run when deciding between the alternative solutions and a commercial arrangement to prop up an emissions intensive generator. Consultation should occur when the government is deciding between low emissions alternative solutions and a commercial arrangement to support an emissions intensive generator.

The Capacity Investment Scheme could be used to help deliver alternative solutions.

Information processes

The consumer benefit assessment proposed should be undertaken and published in all situations – including whether the generator enters into either the Voluntary Negotiated Agreement or the Notice for Mandatory Operation.

Technical and financial due diligence reports are an important step to understand the position of the generator and its ability to serve demand. The consultation paper states that "the OEM Generator technical and financial due diligence report results will be kept confidential to the extent permitted by law as they are likely to include commercially sensitive information."[13] In IEEFA's view, these should be made publicly available to the extent possible, because public money is involved in this proposed framework. In addition, all Prescribed Information should be publicly available to the extent possible. The consumer is proposed to bear the cost of this framework, so consumers should therefore be able to access all the information on the payments and other information required to understand the scheme's operation and the need for it.

The consultation paper also proposes that the AER can direct a technical or financial due diligence report to be undertaken. IEEFA recommends this requirement be extended to all large generators licensed to operate in the NEM, not just those in this framework. As detailed in our report, *There's a Better Way To Manage Coal Closures Than Paying To Delay Them,*[14] the reality is that owners of coal generators are likely to treat these assets as short-term cash cows which will be operated and maintained to optimize returns over a small number of years. This poses the risk that they will become increasingly unreliable and prone to breakdowns that might leave the market short of capacity at short notice. Given these circumstances, there is a need to apply greater scrutiny on operators to ensure they manage

[13] NSW Government Office of Energy and Climate Change. Orderly Exit Management Framework Consultation Paper. December 2023. Page 32.
[14] IEEFA. There's a Better Way To Manage Coal Closures Than Paying To Delay Them. September 2021.

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these plants responsibly to minimize the risk of reliability problems. Or failing that that they at least make it clear to the market and the public that their plant cannot be relied upon and declare a new, more realistic timeframe for the phase down of the plant.

Voluntary Negotiated Agreement

While a negotiated agreement offers the scope for greater flexibility in terms which can be important for such complicated assets, it is incredibly important that any agreement still be subject to a range of criteria and disciplines that will support market efficiency, value for money and integrity. To ensure this, various steps could be undertaken:

- The framework could be more prescriptive on the basic form of the Voluntary Negotiated Agreement.
- There should be a framework for consumer challenge of the decision.
- The cost to consumers should be published more frequently than annually.
- Information on the voluntary negotiated agreement should be publicly available to enable consumers and market participants to understand the scheme, its benefits and costs and how the generator will be incentivized to operate. As the scheme involves public money it should therefore have public reporting.

The Voluntary Negotiated Agreement should enable generators to stop supplying to market once the system is ready – i.e. once new renewables and storage are available. There should be mechanisms in place to provide transparency around this just like under the mandatory framework – i.e. to assess the system needs shortfall and provide updated coal exit timelines.

Notice for Mandatory Operation

4. Noting that generators may operate under complex corporate structures, what are the best means for addressing related entities that provide services that are required for the operation of the System Significant Generator?

This is a challenging aspect of the framework. IEEFA believes that the costs to run the generator at the level needed to maintain reliability should be the only ones addressed in the framework in its currently proposed form.

5. Are there other specific insurances that should be maintained?

No comment

6. What information should be published to the market regarding AER decisions?

IEEFA supports the suggestion that the details around the Notice for Mandatory Operation be published to market. IEEFA notes that the consultation paper says “competitive or commercially sensitive information should not be published”. IEEFA believes that in entering into a Notice for Mandatory Operation, the generator is agreeing to receive payments from the public. Therefore, the generator’s financial and technical parameters become open to public scrutiny. We would encourage as much information as possible to be published to market. This includes as much detail as possible around the Prescribed Information, the AER’s determinations, the financial situation of the generator, and the ongoing cost of the scheme. This should also be published in all situations in which an emissions intensive generator is being subsidised (i.e. also in the Voluntary Negotiated Agreement).

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The consultation paper states that "the AER will assess the System Significant Generator's compliance with its performance obligations at the end of each financial year." In IEEFA's view this should be publicly released in situations in which the generator is under a Notice of Mandatory Operation or a Voluntary Negotiated Agreement or any other similar commercial arrangement. This enables the public to understand what they are paying for and informs the market and planners.

The scheme should report on the full financial outcomes of the generators and/or generating units involved in the scheme regularly. This will allow for the government and the public to have a full understanding of the financial position of generators in the scheme, and how they are being supported.

7. What are your views on the appropriateness of the proposed commercial component outlined in section 10.10?

8. Is an alternative commercial component approach preferred and, if so, why?

9. Are there other key issues that need to be considered as part of the commercial component?

The below information responds to these three questions. We reiterate our earlier comments which explain a financial arrangement to prop open an exiting emissions intensive generator is best avoided due to the risks and pitfalls associated with it. However, if such a mechanism is implemented, we outline our comments below and propose a potential structure for the commercial component.

There may be circumstances upcoming in the NEM in which the market is characterized by periods of feast and famine. The supply-demand balance could vary widely between periods with very plentiful cheap supply (for example due to large surges in solar generation during daytime) and other more occasional periods where supply is very tight (for example when electricity demand is very high and solar or other generation sources are low). In such circumstances there is considerable value in having the coal generator party to the OEMF operating as flexibly as possible so that they do not exacerbate periods of plentiful supply and very low or even negative wholesale prices that will potentially push financial viability problems onto other coal or gas generators.

The goal of an exit contract should be to incentivise the contracted generator to be available to deliver capacity at times when supply shortfalls are likely (if required) while discouraging output at all other times in order to contain emissions and avoid economic distortions. Experience from both Australia and overseas has shown that as the penetration of variable renewables has increased in electricity markets, operators of coal generators have found new and creative ways to operate these plants more flexibly than they have in the past. We acknowledge that coal power plants have some genuine physical challenges around the degree to which they can flex their output which need to be considered in setting the level of payments under an OEMF such that a generator is willing to continue to operate the plant. However, the contract should encourage and allow for operators to come up with innovative ways to run the plant that may mean it operates far more flexibly than it has in the past.

There are an array of options for how this might be done which will need to involve providing payments to the generator which are not tied to how many megawatt-hours they actually

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generate but only how many megawatts they offer for dispatch (and duly deliver if AEMO seeks to dispatch them) during times deemed as being at risk of supply shortfalls. Ideally the generator should be required to mothball the plant outside of the winter and summer high demand periods and also strongly encouraged to curtail output as much as possible during negative price events while still being capable of making the necessary capacity available for the afternoon and evening peak demand periods.

There is no single perfect way to structure payments that will address all the issues and desirable objectives that the government is likely to have, given the considerable engineering and economic complexity of a coal power plant. Ideally, of course, governments should avoid needing to enter into an OEMF (as explored previously). However, below is a set of contract parameters that provide a potential guide for how we might ensure a coal plant is sufficiently compensated to be willing to be available during periods thought to be at risk of shortfalls while minimizing generation when not needed:

- The plant is required to mothball in the months when supply shortfalls are unlikely – for example during much of Spring and Autumn.
- The plant must make available for dispatch a set minimum amount of capacity during hours defined as at risk of supply shortfalls (with potentially some allowance for certain proportion of unplanned outage deemed as statistically likely irrespective of how well the plant is managed) – for example this might be the hours of 4pm until 9pm during winter months. If this performance requirement is not met, for a say a given week or month, then payments are docked.
- For each week they achieve their availability performance requirements they are paid an amount sufficient to steadily build up over a year to cover their expected annual fixed costs plus a profit margin (the profit margin should be set at a reasonable level, reflecting the risks faced by the generator).
- An assessment is made of the variable generating costs the generator is likely to incur per megawatt-hour of generation.
- During the non-mothballed months for all hours of the day, irrespective of whether deemed at risk or not at risk of supply shortfalls, the generator receives fixed payment each week equal to what is assessed to be its minimum stable generation level in megawatts multiplied by their variable generating cost multiplied by the hours of the week. This payment is provided to the generator irrespective of how many megawatt-hours they actually generate, provided they meet their availability performance requirements.
- Any wholesale pool revenues the generator earns during the hours outside the shortfall risk period are provided to the government *except* for negative revenue incurred during negatively priced periods. These negative pool revenues are borne by the operator.
- On the counter side, during the hours deemed as at risk of supply shortfalls, the operator only returns pool revenues to the government up to a value equal to what it received from the government to cover its variable costs associated with operating at minimum generation levels. Any pool revenue above that value is then shared between the operator and the government. We do not have a view about what the appropriate split should be between government and the operator, but the operator

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should be allowed to capture an amount that is expected to provide a very high likelihood of exceeding any negative pool revenues they are likely to incur from negative price events.

- To avoid the OEMF becoming a type of one-sided option that might tempt plant operators to see it as insuring them against losses while granting significant upside, the share of pool revenues the government receives (during the shortfall risk period for when prices go above variable cost) increases as the generator passes defined profitability thresholds.

10. Should the financial model include an additional incentive component, even if small, so that the generator has some incentive to contain costs?

Our proposed structure carries a strong incentive for the generator to contain costs.

11. How should services provided by related entities be treated?

No comment.

12. Should the AER have the ability to "look through" the billing arrangements of services provided by related entities to see the actual costs without mark ups?

IEEFA believes that the AER *should* have the ability to "look through" the billing arrangements of services provided by related entities to see the actual costs without mark-ups.

13. How should the return to the generator be calculated in the case of a swap?

See our proposed structure above.

14. Should there be a 'true-up' settlement in the event that actual capital expenditure and FOM expenses (fixed costs in the case of gas fired generators) differ materially from the ex-ante determination on which payments to the OEM Generator were based?

In a situation in which the generator is getting payments based on its forecasted cost data, it will be important for the AER to receive cost data at the end of the year. This is the plan as laid out in the consultation paper.

IEEFA believes that in this situation the framework should be sure to reconcile any forecasted costs with actual costs, and 'true-up' any discrepancies. For example, if the generator is compensated for an assumed coal cost of $100/tonne but their actual coal cost ends up at $80/tonne, the scheme should 'claw back' the difference, or adjust the next period's allowance by the difference amount, and at the very least, update the next periods forecasts based on the new information.

15. How should the strike price for a cap for a gas-fired generator be determined (e.g., set at a fixed price, linked to the price of gas, or an alternative method)?

No comment.

Further comments on the Notice for Mandatory Operation

Duration of the Notice for Mandatory Operation

The Notice for Mandatory Operation, as per the consultation paper, "should run for no longer than the Minister expects to be required to address a system needs shortfall". In IEEFA's view, ongoing system needs assessment should be undertaken transparently and independent of the Minister that details how much new capacity is needed to fill the shortfall.

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Once the shortfall is filled, the generator should be required to stop operating – even if that happens earlier than originally anticipated. The Capacity Investment Scheme could be used to help drive the replacement capacity required into the system.

The consultation paper states that "There will still be a hard limit that the System Significant Generating Unit cannot be kept open beyond." This needs to be specified as a legally enforceable requirement in the contract.

Operating mode of the Notice for Mandatory Operation

As previously stated, in terms of the operating mode of the generator, IEEFA believes that the OEMF should encourage emissions-intensive generators to produce as little as possible – to ensure reliability but limit emissions and market distortion. The provision of the support payment should be delivered in such a way that the plant does not generate any more electricity than is absolutely necessary to ensure reliable supply.

The consultation paper has identified that the generator could operate in restricted or unrestricted mode. We encourage restricted mode of operation be utilised as much as possible, in line with emissions goals of the jurisdictional and federal governments. Although the contract structure we have suggested effectively creates a strong financial incentive for this to occur.

Cost recovery structure

16. What do you think of using the proposed new transmission cost recovery mechanism compared to the existing distribution network cost recovery mechanism contained in the national electricity rules ("Jurisdictional Scheme")?

Recovering costs through consumers electricity bills could be problematic as it would raise bills – the government should consider including the cost of the scheme on the relevant jurisdictional government budget.

17. Noting the aim of a cost recovery estimate is to even out impact to energy consumers, should the estimation be averaged out over the entire period or allocated as expected by year with a re-estimation every year to correct for any variations?

No comment.

Administration and compliance: OEM Framework review

The consultation paper states that "the AEMC will perform this function and undertake a review of the OEM Framework every five years following the establishment of the OEM Framework." IEEFA believes there should be earlier and more frequent reviews than this, as well as opportunities for consumer challenge of the framework.

Transitional arrangements

The consultation paper states that "Where a scheduled thermal generator has brought forward the closure date of a generating unit between 1 January 2021 and the OEM Framework coming into force… An AEMO assessment of alternative solutions is not required for these generators as consideration may have already been given to possible actions to respond to any closure."

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However, IEEFA believes that the AEMO assessment of alternative solutions should definitely still be undertaken, along with an approach to market to determine if they could provide those alternative solutions and at what cost, along with a public consultation process that outlines the various options and compares them to the cost of the commercial arrangement (e.g. the Voluntary Negotiated Agreement, the Notice for Mandatory Operation or any other similar arrangement).

Alternative model: shielded loss and gain model

18. Would the shielded loss and gain option be a more suitable commercial component approach for the Notice for Mandatory Operation compared to the financial swap approach detailed in the body of the consultation paper?

No, the shielded loss and gain model provides insufficient incentive for the plant operator to innovate to find ways to improve the flexibility of the plant's output. See our earlier comments on parameters for how the generator should be compensated.