

STAGE 2 DISPUTE UNDER CLAUSE 8.2.5 OF THE NATIONAL ELECTRICITY RULES

between

ORIGIN ENERGY ELECTRICITY LIMITED ('Origin')

and

the AUSTRALIAN ENERGY MARKET OPERATOR ('AEMO')**Outline of position of Origin**

The purpose of this document is to provide a high level statement of Origin's position on the key issues that Origin considers arise in connection with the matters set out in the Stage 2 Adviser referral notice of 28 April 2016. This statement is provided on a without prejudice basis and in the absence of detailed submissions from other parties or potential parties as to their position or positions on the key issues that they consider arise in connection with the matters set out in the Stage 2 Adviser referral notice.

Overview of the dispute

1. Terms which are defined in version 79 of the National Electricity Rules (**Rules**) have the same meaning when used in this statement.¹
2. Origin disputes several final statements issued by the Australian Energy Market Operator (**AEMO**) under clause 3.15 of the Rules. A number of those final statements were revised by AEMO since being initially issued to Origin. In those cases, Origin disputes the final statements as revised. The relevant final statements are:
 - a. final statement for week 42 dated 11 November 2015 (as revised on 7 December 2015);
 - b. final statement for week 43 dated 18 November 2015 (as revised on 14 December 2015);
 - c. final statement for week 44 dated 25 November 2015 (as revised on 21 December 2015);
 - d. final statement for week 45 dated 2 December 2015; and
 - e. final statement for week 46 dated 9 December 2015.
3. Specifically, and as set out in this outline of position, Origin considers that AEMO incorrectly derived and applied contribution factors to allocate to Market Participants the costs of local

¹ The period of the South Australian local market ancillary service requirements and the dates of the relevant final statements and adjustments span several version of the Rules (commencing from version 73). However, Origin considers that the changes made between version 73 and version 79 (the current version) are immaterial to the issues relevant to the dispute. Version 79 has therefore been used for the purpose of this statement.

market ancillary service requirements that were in effect in South Australia during October and November of 2015.

4. Origin commenced a “Stage 1” dispute with AEMO under Chapter 8 of the Rules by serving a Dispute Management System (**DMS**) referral notice on the DMS Contact of AEMO on 2 February 2016.
5. The parties to the dispute were unable to reach an agreement during the Stage 1 process and so Origin activated the “Stage 2” process under Chapter 8 of the Rules by issuing a Stage 2 Adviser referral notice on 29 April 2016.

Background to the dispute

6. During the period between approximately 11 October and 10 November 2015, AEMO determined that certain regulating raise and lower frequency control ancillary services (**FCAS**) were to be sourced only from within the South Australian region of the National Electricity Market (**NEM**) (“local market ancillary service requirements”).
7. AEMO has stated that the South Australian-sourced regulating raise services and regulating lower services needed to be acquired on a “pre-contingent” basis to ensure that the power system would be able to return to a satisfactory operating state if a contingency event involving the loss of the Heywood Interconnector occurred.²
8. On 1 November 2015, during a planned outage of the South East – Heywood No. 2 275kV line, the South East – Heywood No. 1 275kV transmission line tripped at the South East end, resulting in separation of South Australia from the rest of the NEM.³
9. The actual cost of acquiring the relevant local market ancillary service requirements for the affected period was approximately \$27 million.⁴ AEMO has stated that the high FCAS prices in South Australia between 11 October 2015 and 10 November 2015 were determined through normal market processes as the marginal value of procuring the 35MW of regulating FCAS in South Australia, noting that the limited number of facilities that could provide FCAS in South Australia resulted in high FCAS prices.⁵
10. The allocation of the costs associated with acquiring regulating raise services and regulating lower services is governed by clause 3.15.6A of the Rules. Specifically with regards to Market Generators, the costs are to be allocated by reference to contribution factors which, pursuant to clause 3.15.6A(k)(1), should reflect the extent to which the Market Generator contributed to the need for these services (essentially a “causer pays” principle).

² Australian Energy Market Operator, ‘NEM – Market Event Report – High FCAS Prices in South Australia: October and November 2015’ (AEMO Market Event Report, December 2015) 6-7.

³ Ibid 10.

⁴ Ibid 11.

⁵ Ibid 11.

11. The costs of acquiring the regulating raise services and regulating lower services during the relevant period were allocated by AEMO to Market Participants with facilities or loads in South Australia.⁶ However, in at least in respect of generators, the contribution factor used to allocate these costs reflected the aggregate of the factors for each individual generating unit within that market participant's portfolio *generally*, as opposed to reflecting an aggregate of the factors for each individual generating unit within that part of the market participant's portfolio in South Australia *specifically*.
12. AEMO later revised its initial allocation after identifying what it says was a non-compliance with the Rules.⁷ This related to the way in which AEMO's settlements system identified which Participant IDs were connected with which Market Participant.⁸ In both cases, AEMO allocated the relevant costs among Market Participants with generating units in South Australia and Market Customers in South Australia. At least with respect to Market Generators, neither the original allocation nor the revised allocation used contribution factors that reflected the generating units comprising the Market Participant's portfolio in South Australia only.

Outline of position of Origin

13. Origin considers that the costs of the South Australian local market ancillary service requirements were not allocated to Market Participants in accordance with the Rules.
14. In relation to the local market ancillary service requirements applying to South Australia during the period 11 October to 10 November 2016, the Rules required AEMO to determine contribution factors for relevant Market Participants specifically in respect of the South Australian region of the NEM which reflected the extent to which the relevant Market Participants contributed to the need for these services. The Rules then required AEMO to apply those South-Australian-specific contribution factors for the purpose of allocating the costs of the South Australian local market ancillary service requirements.
15. Origin contends that the formula in clause 3.15.6A(i)(1) requires a contribution factor to be determined for each of the following in order that the costs associated with the services can be properly allocated:
 - a. costs associated with global market ancillary service requirements;
 - b. costs associated with local market ancillary service requirements in respect of each region or regions where AEMO has determined that such services are required.
16. Further, Origin contends that the contribution factors are required to reflect the extent to which the Market Participant contributed to the need for regulation services. Each of the contribution factors (where relevant) should then be applied to the total amounts calculated for each of

⁶ Ibid 16.

⁷ Ibid 16–17.

⁸ Ibid 16.

these services in respect of the relevant period. Origin considers that the above position gives effect to clause 3.15.6A(h), (i), (j) and (k) of the Rules, as well as the market design principles in clause 3.1.4, and the national electricity objective.

17. In short, Origin considers that in the following formula in clause 3.15.6A(i)(1), the bracketed calculation is to be carried out in respect of the total of all amounts calculated by AEMO for each of the regulating raise service or the regulating lower service in respect of a dispatch interval for global market ancillary service requirements and local market ancillary service requirements for each relevant region or regions using either global contribution factors (in respect of global market ancillary service requirements) or regional contribution factors (in respect of local market ancillary service requirements), where those factors reflect the extent to which the Market Participant contributed to the need for regulation services.

$$PTA = \text{the aggregate of } \left(TSCAS \times \frac{MPF}{AMPF} \right)$$

18. Specifically in connection with the local market ancillary service requirements in place in South Australia during the period 11 October and 10 November 2015, and in the case of Market Generators:

- a. *TSCAS* represents the total cost of acquiring the local market ancillary service requirements in South Australia;
- b. the *MPF* number for each Market Generator should have been derived as the aggregate of the factors for each of the individual generating units in that Market Participant's portfolio in South Australia only; and
- c. *AMPF* is the aggregate of the *MPF* numbers calculated in accordance with b.

19. If Origin is correct as to the above interpretation of clause 3.15.6A(i)(1), but, for whatever reason it is not possible to allocate costs to Market Participants in this manner (including for example, if it is not possible or practicable to calculate contribution factors for a region or regions other than the global region that reflect the extent to which the Market Participant contributed to the need for regulation services), the costs of those services should be allocated across all Market Participants (and not only those with generating units or metered loads in the relevant region, in this case, the South Australian region). This approach is consistent with the market design principles in clause 3.1.4 of the Rules, including clause 3.1.4(a)(8) which provides that:

where arrangements require participants to pay a proportion of AEMO costs for ancillary services, charges should where possible be allocated to provide incentives to lower overall costs of the NEM. Costs unable to be reasonable allocated in this way should be apportioned as broadly as possible whilst minimising distortions to production, consumption and investment decisions.

20. Origin contends that the approach taken by AEMO in deriving and then applying contribution factors that have the effect of allocating the cost of local market ancillary services requirements to Market Participants that have generating units in the affected region but may also have

generating units elsewhere in the NEM on the basis of the whole of their generation does not comply with the market design principles or the national electricity objective.

21. If Origin is incorrect as to the above interpretation, and in the formula in clause 3.15.6A(i)(1), the term *TSFCAS* refers to the total amount associated with the acquisition of regulation services regardless of whether they are global or local market ancillary service requirements, then Origin contends that consistency in the application of the formula requires a single value for *MPF* to be used and a single value for *AMPF* to be used, and that these values are the global contribution factors for all Market Participants, and the aggregate of the global contribution factors for all Market Participants respectively.
22. Further, if Origin is incorrect as to the interpretation set out at 15 to 18 above, and AEMO is only required to determine regional contribution factors where a region or regions have operated asynchronously, Origin contends that AEMO was in error in not deriving and then applying regional contribution factors for the South Australian region that reflected the extent to which Market Participants contributed to the need for regulation services in respect of either or both of the following periods:
 - a. the period of time on 1 November 2015 when the South Australian region of the NEM became electrically separated from the Victorian region of the NEM due to a transmission line trip at the Heywood Interconnector;
 - b. the period between approximately 11 October and 10 November 2015 in which AEMO determined that certain regulating raise services and regulating lower services were to be sourced only from within the South Australian region.
23. Clause 3.15.6A(j)(2) makes it clear that AEMO must determine regionally-specific contribution factors where a region has or regions have “operated asynchronously”. The period of asynchronous operation may be considered to be either the period of time when the South Australian region of the NEM became electrically separated from the Victorian region of the NEM, or the period of time during which AEMO determined that FCAS were to be sourced only from the South Australian region. Regardless of the interpretation adopted, Origin contends that AEMO has not derived and applied contribution factors relevant to the allocation of FCAS to the South Australian region that reflect the extent to which the relevant Market Participants (or at least, Market Generators) contributed to the need for these services. In the case of Market Generators, the contribution factors should have been derived as the aggregate of the factors for each of the individual generating units in that market participant’s portfolio in South Australia.
24. Clause 3.15.6A(j) provides that AEMO must determine, for the purposes of clause 3.15.6A(i),
 - a. a contribution factor for each Market Participant; and
 - b. notwithstanding the estimate provided in paragraph (nb), if a region has or regions have operated asynchronously during the relevant trading interval, the contribution factors

relevant to the allocation of regulating raise service or regulating lower service to that region or regions,

in accordance with the procedure prepared under paragraph (k).

25. Clause 3.16.6A(k) then provides that AEMO must prepare a procedure for determining contribution factors for use in paragraph (j) and, where AEMO considers it appropriate, for use in paragraph (nb), taking into account a number of principles, which include that the contribution factor for a Market Participant should reflect the extent to which the Market Participant contributed to the need for regulation services.
26. AEMO has published a document entitled: *Causer Pays: Procedure for Determining Contribution Factors – “Causer Pays Procedure”* (the “Causer Pays Procedure”).⁹ In respect of Market Generators, Origin contends that this document sets out a procedure for determining contribution factors for individual generating units, which may then be relevantly aggregated to reflect the extent to which the Market Generator contributed to the need for regulation services.
27. Origin contends that the Causer Pays Procedure only sets out a procedure for determining global contribution factors. The Causer Pays Procedure may be considered to set out a procedure for determining contribution factors for individual generating units to be used as an input to determining contribution factors for local ancillary service requirements, but it does not set out a procedure for deriving those contribution factors. In these circumstances, in respect of the period 11 October and 10 November 2015 in which AEMO had determined local market ancillary service requirements for South Australia, AEMO should have applied the Causer Pays Procedures insofar as they were applicable, including in deriving contribution factors for individual generating units, and then, relevantly for generators, aggregated those contribution factors in respect of generating units in the South Australian region.
28. AEMO has published a document entitled: *Efficient Dispatch and Localised Recovery of Regulation Services Business Specification* (“Business Specification”).¹⁰ The Business Specification notes that an expected benefit of the project being undertaken by AEMO to satisfy the changes to the Rules to provide for cost recovery of localised regulation FCAS on a regional basis is the implementation of a NEM-wide solution that enables the cost of local regulation FCAS requirements to be recovered from those Market Participants who had both the capacity and the ability to mitigate their liability at the time the requirements were required.¹¹ To the extent the worked example provided in section 7.2 of Appendix B indicates that localised recovery of regulation services will be effected by using global contribution factors for Market Participants in the regions requiring those services, Origin contends:

⁹ AEMO, *Causer Pays: Procedure for Determining Contribution Factors – “Causer Pays Procedure”*, Document No. 160-0379, Version 4.0, 1 December 2013 (effective date 15 December 2013).

¹⁰ AEMO, *Efficient Dispatch and Localised Recovery of Regulation Services Business Specification*, Document No. 160-0392, Version 1.01, 1 July 2010 (effective date 1 July 2010).

¹¹ *Ibid* 7.

- a. the Business Specification does not constitute a procedure for determining contribution factors and is not relevant to AEMO's determination of contribution factors for the purposes of clause 3.15.6A(i);
- b. even if the worked example could be considered to be relevant to AEMO's determination of contribution factors, it should not be followed as it is inconsistent with the requirements of the Rules and the Law (including clauses 3.15.6A(k)(1) and 3.1.4(a)(8) of the Rules and the national electricity objective), as well as the stated intent of the Business Specification.