

20 October 2014

Mr George Huang
Australian Energy Market Operator

By email: vcr@aemo.com.au

Dear George

VCR Applications Guide

The Major Energy Users (MEU) congratulates the Australian Energy Market Operator (AEMO) on the detail it has gone to in order to develop more accurate Values for Customer Reliability (VCR) in the electricity market. Further, the MEU welcomes the opportunity to provide its views to the request for consultation on the draft VCR applications guide.

The development of the VCR process demonstrates there is a wide diversity of views about the value of customer reliability. The fact that there are such widely divergent values between the basic sector allocations (residential, agriculture, commercial, industrial and direct connect) and between the various sizes of customer (small, medium and large), shows that great care must be taken to ensure that the outcomes are not seen as definitive but are an average with quite significant diversity.

Despite the fact the AEMO has devoted considerable resources to identifying a range of VCR outcomes depending on region, customer type and size, the MEU is very concerned that there is a view that the answer is "close to perfect". In reality what the AEMO has generated is an approximation and should not be seen as anything else. Understanding this then impacts considerably on how the values should be applied.

Annual indexation

Because the VCR is only an approximation, it makes little sense that the value should be adjusted using an annual inflator to retain its "real" value. To imply such exactitude to the value implies that the answer obtained from the survey has a degree of exactness that is simply not there.

There is little doubt that over time the VCR will change and the assumption made by proposing to use a cost price inflator is that it will continue to increase. In contrast, with the changing of the electricity market that has been evident for the past 3-5

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years and the potential for new technology and the changed uses of electricity that have been seen and are forecast to occur, means that the VCR could conceivably fall over time. There has certainly been a significant fall in VCR from the most recent (2008) assessment made by AEMO and an even greater fall since the 2012 assessment for NSW made by Oakley Greenwood for the AEMC. Whether these falls were the result of better surveying techniques, changing consumer views, changes in the market or a combination of all is uncertain - what is certain is over time there have been quite dramatic shifts in the assessed VCRs and that in this recent review the overall value has fallen considerably.

The MEU considers that rather than artificially inflating values which are only approximations, the MEU considers the values should be held at their current levels and there be a similar review within a set period of time. This approach recognises the reality of approximate nature of the outcome and the potential that there will be more change over time and the impact of these changes need to be reflected in new assessments.

Deriving locational VCRs

The MEU supports varying VCRs with location but seeks clarification as to what is meant by "location". The table 4 implies that the location refers to regions and the MEU accepts that VCRs will vary between regions to reflect the make up of how electricity is used in each region.

However section 4 in the draft guide implies that location also refers to where in the supply chain a user is connected and breaks down location into connection at generators (level 3), connection into the transmission system (level 2) and connection into the distribution system (level1).

The MEU is concerned that the level 1 connections are extremely broad and treats a large user connected into the subtransmission part of the distribution network (eg connected at 33kV or 66kV and close to the transmission system) the same as a residential connection provided deep in the network at 415V. The assessments made of the different classes of user would imply that a user connected into the subtransmission network would have a similar VCR to a user connected to the transmission network rather than that of a residential user. Table 2 supports this assessment as VCR tends to decrease the larger the user is¹.

The MEU notes that there is a massive variation between VCRs for a user connected to the transmission network (most likely a large industrial user) and a large industrial user connected into the distribution network. As a user connected at distribution subtransmission level is more likely to have very large operations similar to a user direct connected to the transmission level², the MEU considers that a further subdivision could be made for VCRs for users connected at distribution subtransmission and even for zone substation connections.

¹ A larger user would most likely be connected closer to the transmission system

² Any difference in the connection point is most likely a result of history and the decision on classifying transmission and distribution in each region

AEMO goes on to consider the weightings that should be given to different types of outages, demand, consumption, etc. or even different types of feeders. The MEU considers that certainly different types of feeders should have different VCRs as noted above, and that the weighting of the VCR should reflect the make up of those customers connected to the feeder.

The issue as to the basis on which weighting should be applied is vexed. As a default position, the MEU considers that, as for the allocation of cost for the provision of networks should be based on the demand each user imposes on the network, the share of the peak demand should be the basis for weighting VCR.

AEMO contemplates that USE (ie the amount of unserved energy) each user incurs could also inform the weighting of VCR. The MEU is not convinced that this is equitable. For example, should similar users on a feeder in a high risk region of the network (where USE might be high) but paying the same price as users on a feeder in a low risk part of the network (where a low USE is more likely) have the same VCR or a higher VCR? This is unlikely and so USE might not be an appropriate approach for weighting VCR.

The MEU agrees with AEMO that the issue of weighting needs more investigation

Network planning

The MEU considers that the main value for the application of VCR lies in network planning and the MEU agrees with the AEMO assessment as to how VCR should inform the planning processes.

The MEU agrees with the AEMO approach on:

- How to accommodate losses
- Using VCR in assessing investments in replacement assets
- Guiding distribution and transmission reliability standards.

Other uses

The MEU notes that AEMO has highlighted that VCRs can be used to influence outcomes for other activities in the NEM, such as reliability settings and load shedding schedules. The MEU accepts that the VCRs might be useful for such purposes but the MEU also considers that AEMO needs to highlight the inexact nature of the VCR development as this will impact greatly on the versatility of the assessed VCRs.

The AEMO quite rightly notes (page 24)

"The VCR review provides information which might assist such a consideration but the data cannot be easily linked to the actual VCR of those customers who will be interrupted in events of supply inadequacy, as these may be sub-regional shortfalls with a different demand composition to the NEM average. It should be noted that

customer VCRs fall over a wide range, segmented by customer activity, size, and location."

The MEU agrees with this observation and considers that AEMO should reinforce the limitations inherent in the development process used for assessing VCRs. As noted in the introductory paragraphs to this submission, the VCR is, at best, only an approximation and to assume that the value derived is a definitive assessment of what all consumers are willing to pay for reliability would be a courageous assumption indeed.

The AEMO, in its final report on the VCR development³, in sections 2.6 and 2.7.2, provided a number of observations where the surveying of customers was less than optimum and, as a result, there is a need to take care in assuming the outcomes can be used too widely. This means that if there are other tools available to assess the needs of consumers then these too should be used in addition to the VCR to ensure that the long term interests of consumers are achieved as outlined in the National Electricity Objective.

We appreciate the opportunity to have provided this input into the AEMO review. Should you wish for amplification of any of the comments provided, we would be pleased to expand on our views.

The MEU is keen to continue to be involved in this review and we request that you keep the undersigned aware of future discussion and request for further stakeholder involvement on this review.

Yours faithfully

A handwritten signature in black ink, appearing to read "David Headberry". The signature is written in a cursive style with a checkmark at the end.

David Headberry
Public Officer

³ AEMO, Value of Customer Reliability Review, Final Report, September 20104