



EnergyAustralia

LIGHT THE WAY

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Dear Commissioners,

AEMC 2018, Participant compensation following market suspension, Consultation Paper, 17 May 2018

EnergyAustralia is one of Australia's largest energy companies with over 2.6 million electricity and gas accounts in NSW, Victoria, Queensland, South Australia, and the Australian Capital Territory. We also own and operate a multi-billion dollar energy generation portfolio across Australia, including coal, gas, and wind assets with control of over 4,500MW of generation in the National Electricity Market (NEM).

We welcome the opportunity to comment on the AEMC's consultation paper on *Participant compensation following market suspension* rule change proposal (the consultation paper). This rule change proposal builds on the already complete rule change, *Pricing during market suspension*,¹ which simplified the process for setting prices following the suspension of the spot market. We are supportive of the development of a compensation framework that balances the costs to consumers with the requirement to incentivise generators to participate in power system restoration and operations limiting the need for AEMO to direct participants.

Issue with current methodology of the market suspension pricing schedule

The current issues of operating the power system during market suspension, particularly when prices are being set using the Market Suspension Pricing Schedule (MSPS) are highlighted in the consultation paper. Although the suspension of the spot market is a rare event (only occurring twice since the commencement of the NEM), the implications of an insufficient pricing and compensation framework can be significant.

We would like to understand what the original drivers for the current methodology for determining the MSPS were. Under the current MSPS, there exists the potential of unmanageable risks being imposed on market participants (MPs). As an example, consider a MSPS that has a number of high priced trading intervals due to high prices in the preceding weeks within the 28-day calculation period of the MSPS.² In this case

¹ AEMC Final determination, <https://www.aemc.gov.au/rule-changes/pricing-during-market-suspension>

² <https://www.aemo.com.au/Electricity/National-Electricity-Market-NEM/Emergency-Management/Guide-to-Market-Suspension-in-the-NEM>

AEMO has begun to dispatch the market using participants' bids, however prices are still being set by the MSPS. Generators would therefore be incentivised to generate as much as possible (leading to disorderly bidding). This could mean that participants are potentially unable to generate at levels high enough manage their exposure to the MSPS (although they would be helping AEMO to avoid having to intervene and direct participants in the market).

Under normal market operations, additional generation bidding at low prices (for example at the market price floor) would have the effect of displacing higher priced generation and reducing the market price. As the concept of price sensitivities is not present in the MSPS this does not occur. Considering the other extreme, a MSPS that had a number of negative pricing intervals, this could further compound the issue of AEMO needing to direct the market more than necessary to maintain system security.

These extremes could be managed by placing a cap and floor on prices in the MSPS from the outset to avoid inefficient outcomes resulting from extreme high or low prices in the preceding weeks within the calculation period. For example, a market cap of \$300/MWh and floor of -\$300/MWh.

A MSPS that is more reflective of current market conditions at the time of suspension and, at the very least preserves some of the pricing signals and outcomes that generators and loads usually respond to, would improve the operation of the power system during market suspension. As we highlighted in our submission to the consultation paper on *Pricing during market suspension*,³ there could be benefits in retaining other pricing options (e.g. pre-dispatch pricing or neighbouring-region pricing) for AEMO to utilise where they provide the most suitable pricing method for the market conditions.

Proposed administer pricing provisions compensation framework

We acknowledge the challenges in developing a compensation framework that incentivises generators to participate voluntarily in market restoration and operation during market suspension (and not await direction), while also minimising additional costs to consumers. In its current form, the market suspension framework provides no avenue for participants to claim compensation if the price they're receiving under the MSPS does not cover their costs. This incentivises generators to withdraw from the market and await direction to ensure they have an avenue and some certainty to claim compensation for their costs.

The rule change, outlined in the consultation paper proposes using the administered pricing provisions (APP) to provide a way for participants to claim compensation during market suspension. Under these arrangements, participants would be able to lodge a claim to the AEMC for compensation relating to direct and opportunity costs. The current rules require that claims for compensation under APP are determined on a case by case basis by the AEMC and currently are completed manually offline. This contrasts with the direction compensation framework administered by AEMO's which is a partially automated process.

³ <https://www.aemc.gov.au/sites/default/files/content/8368de5c-64b3-4fa2-bfd7-2cdd2e7df409/RuleChange-Submission-ERC0224-EnergyAustralia-170912.PDF>

While adopting the APP approach would provide a way for participants to claim compensation we would like to understand the initial drivers for placing the obligation on the AEMC to determine compensation claims. As identified in the consultation paper, the AEMC has limited experience in determining these compensation claims and does not have an established business process for administering the payments. We see that AEMO may be better placed to process compensation claims under the APP framework as they currently manage compensation processes and claims under directions.

Further, the rules in their current form provide discretion to the AEMC to recover costs associated with processing a compensation claim under the APP. We believe that if the APP compensation framework was to be extended as a solution for additional compensation under market suspension then this additional uncertainty of costs associated with processing claims may still incentivise participants to await direction.

Under the APP compensation framework there is no ability to use prior decisions to inform later claims. This contrasts with the direction compensation framework where if a fair payment price is determined by an independent expert then this is to be applied to any direction relating to that service for the following 12 months. This creates inefficiencies in the administrative burden to process participants claims under the APP compensation framework. It may also discourage participants from voluntarily participating in the market as there still exists uncertainties about what costs can be recovered.

Extension of the direction compensation framework

As highlighted in the consultation paper there appears to be no one size fits all solution to a compensation framework that balances both the need to minimise costs to the consumer but also provide certainty to generators. As identified by the AEMC, any compensation framework must be designed so as not to create new incentives leading to similarly perverse outcomes. An option may be to extend a form of the directions framework, namely compensation paid to generators based on the 90th percentile price or some equivalent considering revenue already received from the pool under the MSPS. Although there may be times where this can increase the cost to the market; for example, a low MSPS well below the chosen percentile prices. An additional compensation framework may still be required to be in place to allow participants to claim reasonable costs not covered by the percentile price. Though providing additional certainty through a percentile based payment would likely limit the number of times this additional framework was required.

We are supportive of a semi-automated compensation approach that draws on elements of the current direction compensation framework. This not only limits the administrative burden and costs in the calculation of any compensation during market suspension but will also provide more certainty and transparency to the market participant that their reasonable costs will be recoverable.

Promote restoration of normal market operations

The challenges discussed in the consultation paper show the complexities of developing an appropriate compensation framework for operation of the market during suspension. The operational issues experienced during the South Australian market suspension in 2016 highlight the importance of restoring the suspended region to normal market

operations as soon as possible. The earlier final rule change, *Pricing during market suspension*⁴ has simplified the process for AEMO to resume the operation of the spot market and should mean an extended period where the market must be suspended can be avoided.

In conclusion, EnergyAustralia supports the intent of the rule change, provided it finds the right balance between additional costs to the consumer while providing certainty that generators have a mechanism to recover their costs. The rules should promote the restoration of the spot market as soon as possible and avoid extended periods where the MSPS is used to settle the market.

If you would like to discuss this submission, please contact Andrew Godfrey on 03 8628 1630 or Andrew.Godfrey@energyaustralia.com.au.

Regards

Melinda Green

Industry Regulation Leader

⁴ AEMC Final determination, <https://www.aemc.gov.au/rule-changes/pricing-during-market-suspension>