



Charles Popple
Chair, Reliability Panel
c/- Australian Energy Market Commission
GPO Box 2603
Sydney NSW 2000

Lodged online at: www.aemc.gov.au

7 July 2022

Dear Mr Popple,

2022 Reliability standard and settings review Draft Report (REL0082)

ENGIE Australia & New Zealand (ENGIE) appreciates the opportunity to respond to the Reliability Panel (“the Panel”) in response to the 2022 Reliability standard and settings review Draft Report (“the Draft Report”).

The ENGIE Group is a global energy operator in the businesses of electricity, natural gas and energy services. In Australia, ENGIE has interests in generation, renewable energy development, and energy services. ENGIE also owns Simply Energy which provides electricity and gas to more than 740,000 retail customer accounts across Victoria, South Australia, New South Wales, Queensland, and Western Australia.

The implications of recent events

Concerns about reliability have been elevated in recent weeks due to the cumulative price threshold being progressively reached in multiple regions and the subsequent imposition of the administered price cap, which led in turn to market suspension. ENGIE recognises that this occurred subsequent to the publication of the Draft Report but nonetheless it has provided a contemporary “real world” test of some of the reliability settings that the Panel can and should take into account in its final report.

Importantly, the market stresses due to an unusual confluence of factors creating a genuine limitation on *energy* (rather than capacity per se) did not result in any forced load shedding. However, the evident market dysfunction arising from the administered price cap is clear evidence that this needs to be set at a higher level.

The Panel’s decision to exclude consideration of the impact of a capacity market is a prescient one. While the political momentum to implement some form of capacity instrument has grown following the market suspension, there is still extensive debate about the form, whether existing plant can participate and whether some technologies may be excluded. In the latter case there are signs that the outcome may vary by jurisdiction.

Accordingly, the only robust assumption the panel can make is that market participants will continue to be reliant on energy market revenues to underpin new or refurbishment investment in plant. ENGIE remains supportive of the energy only market's ability to signal the optimal plant mix, including the level and type of variable renewables (VRE), and of storage. No other instrument is likely to have the time granularity of price signals that is necessary to co-optimize VRE and dispatchable capacity. In particular, it's the most effective instrument for providing investment signals of the relative values of different durations of storage.

Reliability standard

ENGIE notes that the draft report reconfirms unserved energy (USE) as the preferred metric while leaving open the option of multiple metrics.

As noted in our submission to the issues paper¹, ENGIE considers that the form of the standard should remain a probabilistic one. Given the increasing role of weather-dependent renewables, a deterministic standard is inappropriate. A minimum reserve-based standard is also poorly compatible with a system that is expected to have increasing capacity of storage. A battery is a reliable contributor when it is fully discharged but not when it is discharged, so the duration of scarcity events is an important consideration.

In this light, ENGIE understands the Panel's concern that the expected USE metric may not adequately capture tail risks. However, the Panel's "straw person" option to address this concern is highly dependent on value of w (customer risk aversion). This appears even harder to obtain a robust estimate for than the Value of Customer Reliability (VCR) and so it is not clear how the Panel will determine an appropriate value. If the Panel selects a value that is in fact, materially wrong, then the approach will not be an improvement on the current approach of focussing on USE.

Reliability settings

There are multiple ways to interpret the introduction of additional reliability mechanisms over and above the existing EOM settings. One is that the energy transition is stretching the functioning of the EOM to breaking point. Another is that - with the benefit of hindsight - key reliability settings such as the market price cap (MPC) and cumulative price threshold (CPT) have been set too low for too long, and these additional mechanisms have been set to compensate for that. The RERT/interim reliability reserve is a case in point. This has been activated each summer since 2017/18, and the effective cost/MWh was typically higher than the market price cap (though below the value of customer reliability). This carries some implication that reliability could be more efficiently met through in-market resources incentivised by a higher MPC and CPT.

Market price cap (MPC)

ENGIE notes the Panel's conclusion that the IES modelling exercise demonstrates that "maintaining existing levels of the MPC/CPT may...lead to an increase in USE". ENGIE encourages the Panel to satisfy itself that its choice of MPC will robustly signal the value of new investment in the NEM and agrees that it should contemplate a step change increase such as that indicated by the Panel's indicative range of \$21,000-

¹ [Submission to the 2022 Reliability standards and settings review Issues Paper](#), ENGIE, March 2022

\$29,000 MWh. ENGIE also agrees with the Panel’s observation that “a significant increase in the MPC and CPT doesn’t automatically cause a material increase in consumer bills” and observes that wider communication of the implications of changes to the reliability settings will be a critical factor in acceptance of the Panel’s final report.

Cumulative price threshold (CPT)

ENGIE recognises that the CPT serves a purpose but has consistently argued that the CPT should be decoupled from the MPC. Arguably the CPT should be set at a level which manages cascading default risk within the market. This issue was previously explored as part of the NEM Financial Resilience Review.

The panel should also consider how a CPT (or similar backstop for extreme prices) can be designed to be compatible with reliability requirements during renewable droughts. In this light it is instructive to note that at the time of writing, Queensland is close to triggering the CPT for the second time in a month. While this does not in itself demonstrate that the CPT is set at the wrong level, it is clear that the energy transition, combined with a global scale price shock, is stress-testing this and other key reliability settings. This increases the case for considering it as an independent setting, rather than a direct outworking of the MPC.

To that end ENGIE appreciates the willingness of the Panel to contemplate a CPT which is greater than 7.5 hours of cumulative MPC price levels and that its modelling has examined trade-offs between different combinations of MPC and CPT.

A recent publication by the Australian Energy Council² outlines the need for the energy transition to deliver adequate dispatchable capacity that can operate for extended periods when renewable output is low, as a complement to the variable renewables and short-term storage that are anticipated to make up the majority of future generating capacity. An adequate CPT will be a key investment signal for this type of capacity as coal plant exits, and the other settings will not necessarily incentivise this type of capacity.

Market floor price (MFP)

The Panel notes that “there are relatively few periods where the MFP binds” following relevant rule changes such as five-minute settlement. This should be sufficient to rule out a reduction (i.e., a higher negative figure) in the MFP, including via indexation, for the current review.

ENGIE reiterates its views set out in our response to the issues paper³ that there is scope for the Panel to increase the level of the MFP (i.e., to a less negative figure). The market will still typically clear, but the absence of very low negative prices may assist the transition. Generation and contracting trends are reducing the volume of plant that might bid the price down towards the floor.

Administered Price Cap (APC)

Recent events in the NEM have borne out ENGIE’s contention in our response to the Issues Paper⁴ that the current level of \$300/MWh is unlikely to be reflective of the marginal cost of new generation at times of

² [Australia’s energy future – zero emissions dispatchability](#), AEC, April 2022

³ [Submission to the 2022 Reliability standards and settings review Issues Paper](#), ENGIE, March 2022

⁴ Ibid.

supply scarcity. The market proved itself unable to function effectively under the APC, not just because it obliged some generators to run at a loss (based on marginal fuel costs - while ENGIE recognises that some participants may be receiving fuel under longer-term contracts, it is the marginal cost of fuel that drives efficient resource allocation under scarcity). It served to mute the price signal to an extent that made it extremely hard for energy-constrained resources such as batteries, hydro and some coal plants to effectively signal their constraints or for the market price to signal when their energy would be most valuable.

Longer-term price signals are also emerging that suggest the APC needs to be set higher, as cap contracts at strike prices materially high than the traditional \$300/MWh are emerging in the contracts market.

In this light, it is disappointing that the Panel is not proposing to increase the APC. ENGIE strongly reiterates its view that the Panel should give consideration to both a one-off increase and ongoing indexation of this price. There is clear evidence that the risks of setting this cap too low outweigh that of setting it a little higher than may be necessary. The Panel's observation that current fuel costs "do not reflect a structural change" rather misses the point. The APC is likely to be applied in extreme cases, so the "structural" level of expected future fuel costs is not the benchmark. Price caps in the facilitated gas markets are a more relevant benchmark in considering the appropriate level of the APC.

Should you have any queries in relation to this submission please do not hesitate to contact me on, telephone, 0477 299 827.

Yours sincerely,



Jamie Lowe

Head of Regulation,
Compliance and Sustainability