AMENDING THE ADMINISTERED PRICE CAP – PUBLIC FORUM

16 AUGUST 2022

BENN BARR, CE, AEMC
APC PROJECT TEAM

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During this meeting, attendees **must not discuss, or reach or give effect to any agreement or understanding**, which relates to:

- **Pricing** for the products and/or services that any member supplies or will supply, or the terms on which those products and/or services will be supplied (including discounts, rebates, price methodologies)
- **Targeting (or not targeting) customers** of a particular kind, or in particular areas
- **Tender processes** and whether (or how) they will participate
- Any decision by attendees about the purchase or supply of any products or services that other attendees also buy or sell, to not engage with persons or the terms upon which they will engage with such persons, or to deny any persons access to any products, services or inputs they require
- **Sharing competitively sensitive information** such as non-publicly available pricing or strategic information
- **Breaching confidentiality obligations** that each member owes to third parties

OPENING REMARKS

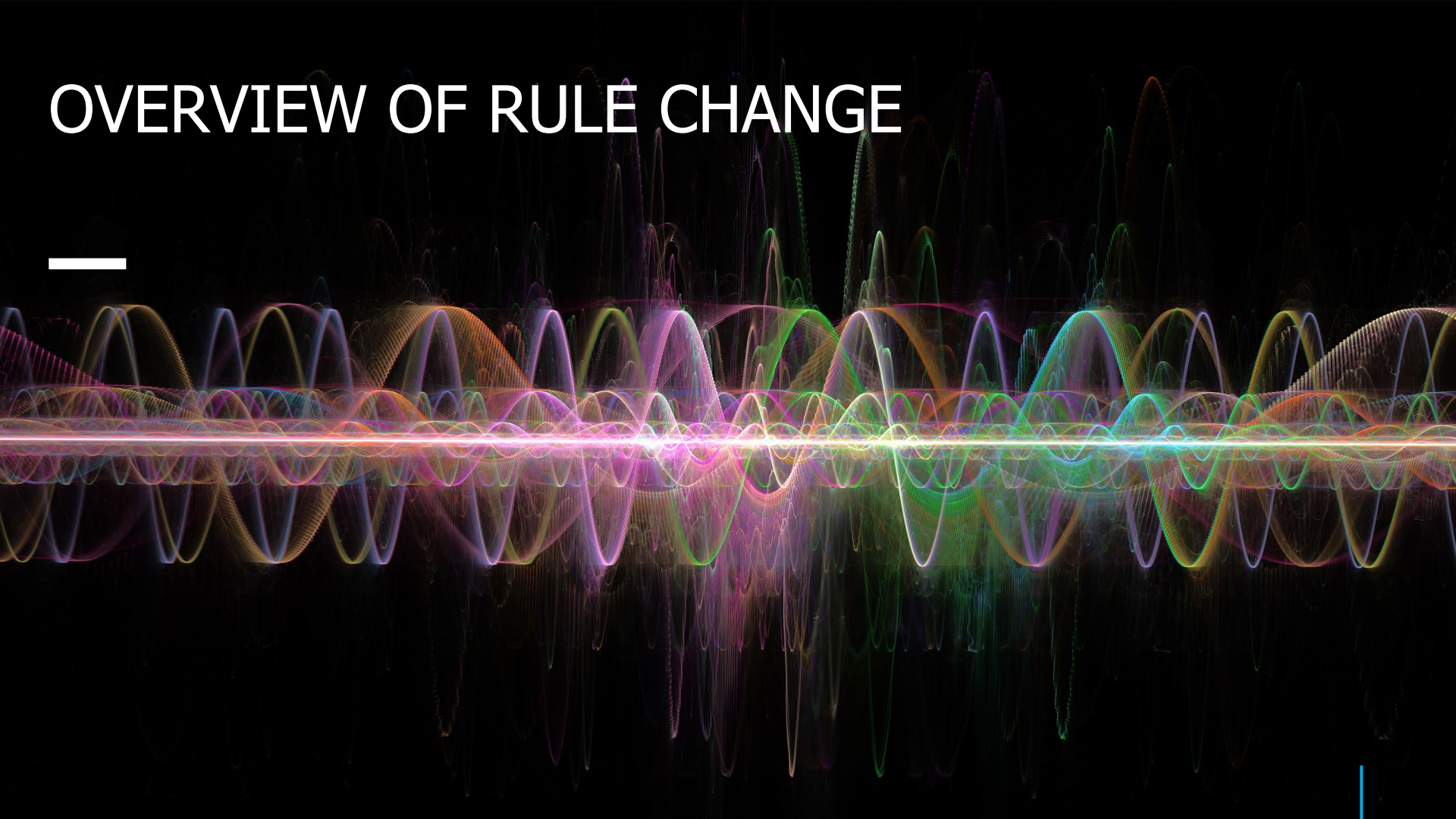
BENN BARR, CE

Agenda

Outline	
1.	**Opening remarks**
2.	**Overview of rule change**
3.	**Issues for consultation**
4.	**Questions**
5.	**Concluding remarks**

Questions throughout forum can be entered in the Q and A function, and upvoted.

OVERVIEW OF RULE CHANGE



Overview of the rule change

- On July 1, Alinta Energy submitted a rule change request to the AEMC. The rule change request seeks to amend the administered price cap (APC) to mitigate ongoing threats to the reliable operation of the NEM.
- Alinta's rule change request proposed an increase in the APC from $300/MWh to $600/MWh in every NEM region, with a sunset period of 12 months or a suitable period as determined by the AEMC with consideration of other processes underway, such as the 2022 Reliability Standard and Settings Review.
- In Alinta's view, this will help meet the long-term interests of consumers and ensure the most efficient operation of the market.
- The proposed rule aims to address the significant increase in the SRMC of most generators in the NEM driven by recent high commodity prices, which may continue for some time.
- The rule change will aim to create a more predictable, transparent and stable market environment.

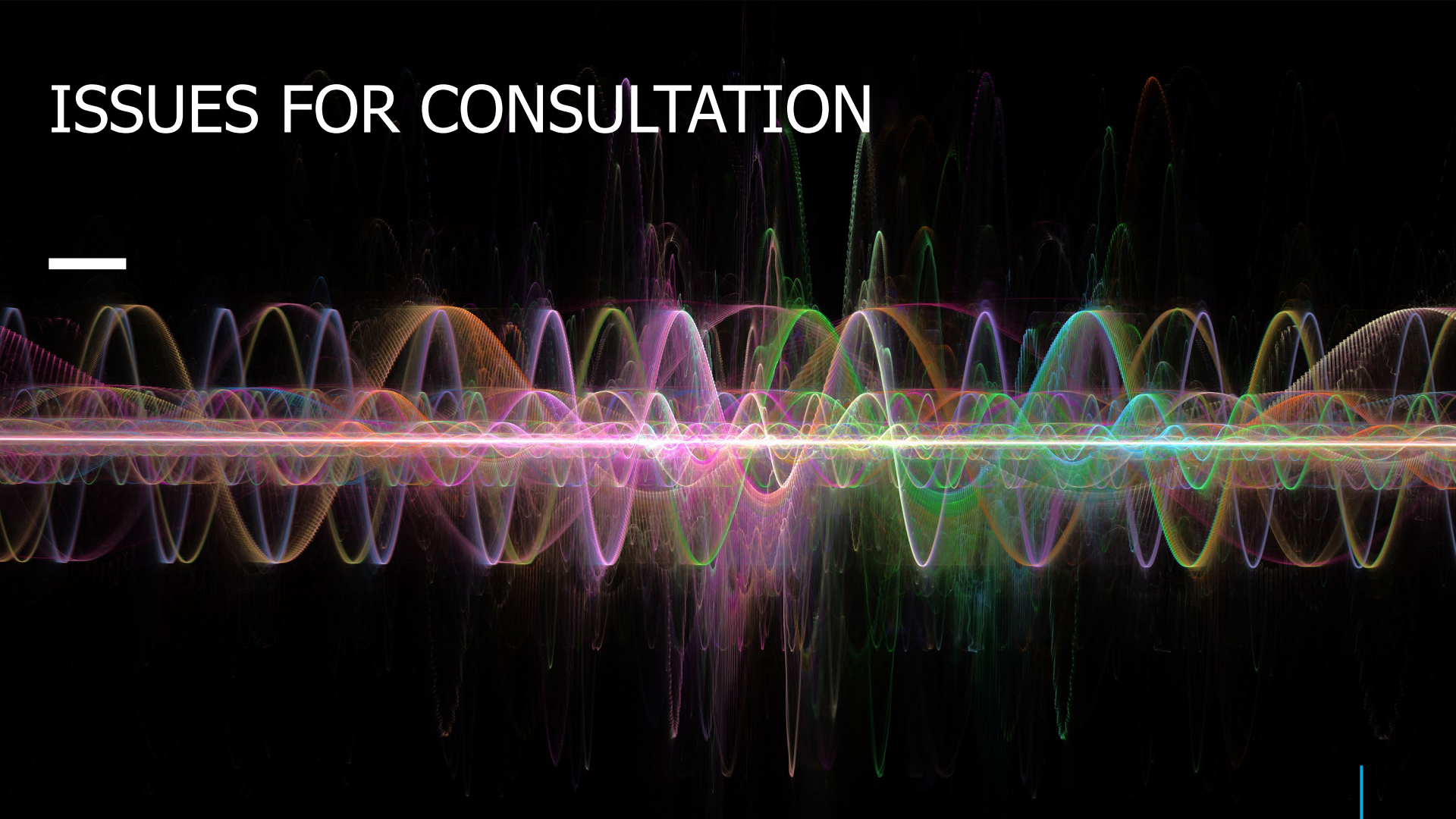
Urgent rule change

- Alinta requested that the proposed rule change proceeds under the expedited process as **urgent** under s. 96 of the NEL.
- An urgent rule means a *rule relating to any matter or thing that, if not made as a matter of urgency, will result in that matter or thing imminently prejudicing or threatening—*

  (a) the effective operation or administration of the wholesale exchange operated and administered by AEMO; or

  (b) the safety, security or reliability of the national electricity system.
- The Commission consider that the rule change meets the definition.
- Stakeholders can object to the rule change being made under an expedited process but must to do so by 18 August 2022.
- To be valid, an objection should set out the reasons why the rule change request is not an urgent rule.

ISSUES FOR CONSULTATION



Definitions of key terms discussed in the consultation paper

- Cumulative Price
  - The rolling sum of the previous 2016 spot dispatch prices in each region
  - based on the spot price determined from dispatch offers or the suspension price during a market suspension.
- Cumulative Price Threshold
  - Provides a circuit breaker/safety net to control costs to retailers and risks to generators
  - ~ 90 times the market price cap and indexed to the market price cap
  - Currently $1,398,100
- Administered Price Period
  - dispatch intervals when the cumulative price is above the CPT and the APC is applied.
- Administered Price Cap
  - The cap on dispatch prices during an administered price period
  - Currently $300/MWh

The problem the rule change seeks to address

- Generator inputs costs - gas, coal and liquid fuel prices - have risen materially over the last 12 months. Domestic gas prices have traded at or close to gas APC for extended periods. Export coal prices at historic highs. Liquid fuel prices also high. Other changes reduced the available capacity to the market, higher customer demand due to cooler than expected winter conditions, lower than average wind and solar output, high amount of planned and unplanned outages.
- In June, high prices, and continued issues with generator availability exceeded the CPT in all NEM regions, except Tasmania.
- The APC was then applied and available capacity further reduced during APP.
- On 15 June 2022, AEMO suspended the market as it determined that it was impossible to operate the spot market in accordance with the market rules and the significant number of directions that were being issued materially elevated power system security and reliability risks.
- The APP and market suspension drove additional unhedgeable costs for retailers that will ultimately by paid by consumers. Those costs include:
    - APC compensation
    - Reliability and Emergency Reserve Trader (RERT) costs
    - Directions compensation
    - Market suspension compensation
- While forward prices are difficult to forecast, projections of international gas prices suggest elevated prices will remain for the foreseeable future. (ACCC LNG netback above $40/GJ until March 2024 – ACCC 1 August update)

The benefits and impacts of a change

- Greater availability of dispatchable generating capacity, during the APP, provides a number of key benefits:
  - Greater system security and reliability and a reduced need for directions from AEMO to maintain system security and reliability
  - Less supply scarcity during APP, bids more reflective of costs, better price signals for batteries and hydro storage that rely on price volatility.
  - Lower risk and magnitude of unhedgeable costs for retailers and consumers. These costs include RERT, APC compensation, directions and market suspension compensation.
  - May drive greater hedging
- There are risks of additional costs for consumers
  - Higher wholesale spot prices, during APP
  - Higher contract prices, reflecting greater spot exposure under a higher APC
  - Administrative costs and uncertainty in the contract market with a new APC, need for new instruments, impact on existing contracts.
- The extent of retailer and consumer hedging is a key consideration to any potential change is applied.
- Further analysis is underway on the interaction between the net benefits to consumers of energy and the hedging level.

Retailer hedging is key to assessing the impact on consumers of electricity

- Hedges provide generators and retailers with revenue and cost certainty.

During the APP	Fully hedged retailer	Un-hedged retailer	Spot exposed customer
Higher APC	+ Hedges cover APC + Less compensation cost	- Higher prices for electricity during APP + Less compensation cost	- Higher prices for electricity during APP + Greater signal signals to respond (provide demand response) + Less compensation cost
Lower APC	+ Hedges cover APC - More compensation cost - Lag in cost recovery from consumers	+ Lower prices for electricity during APP - More compensation cost - Lag in the cost recovery from consumers	+ Lower prices for electricity during APP - Smaller signal signals to respond (provide demand response) - More compensation costs

- Not being hedged does not seem a sound retailer strategy in a volatile market
- All things being equal a fully hedged retailer appears better off under a higher APC
- Spot exposed customers can effectively manage higher prices
- We are investigating the effect of different levels of contracting vs APC and compensation costs.

The contract market may need to adjust to any new level

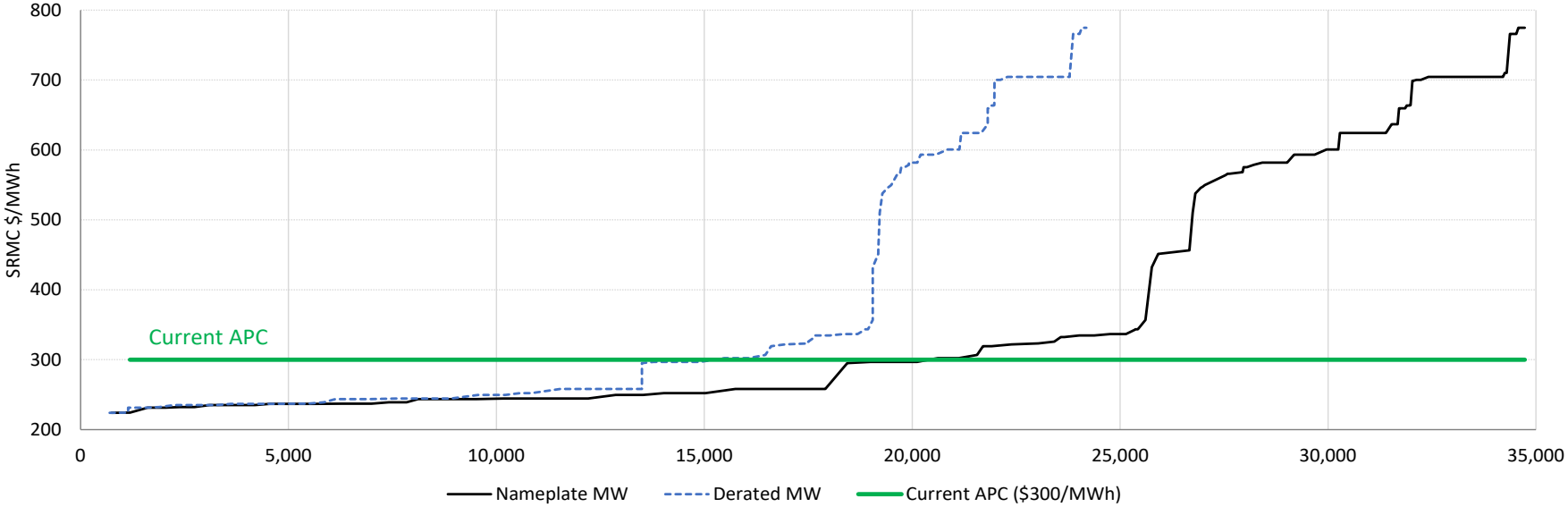
- How might a change to the APC and CPT affect contracts?
  - Retailers typically assess their contract position and strategy with regard to many factors outside their load volume and profile, including the value at risk from high spot prices.
    - Does the CPT triggering a higher APC, increase the value at risk?
    - How does a change to the APC and/or CPT fit into that value at risk consideration?
    - Are potential changes in the value of contract market instruments material?
  - Incentives remain for generators to contract for the sale of electricity and if the APC rises to purchase fuel to support cap contracts.

The interaction between the APC and generator costs

- The APC needs only to cover the generator's SRMC so they are financially viable and willing to generate
- Recent experience of generators withdrawing from the market during the APP:
  - Gas prices have varied widely and triggered the gas APC of $40/GJ, but prices reached ~$75/GJ before that was applied.
  - Generators are likely to hold gas contracts to mitigate gas spot variations.
- Generator plant efficiencies:
  - Broad range of potential performance outcomes – particularly at part load.
  - OCGT plant typically lower efficiency than some other forms of gas generation.
  - ERAWA used a distillate price of $36.42/GJ (less than the gas APC) but a heat rate of 24 GJ/MWh
  - Other sources showed ranges from 13.5-15 GJ/MWh and a 4-5% additional penalty on distillate (14.5-16.7 GJ/MWh)

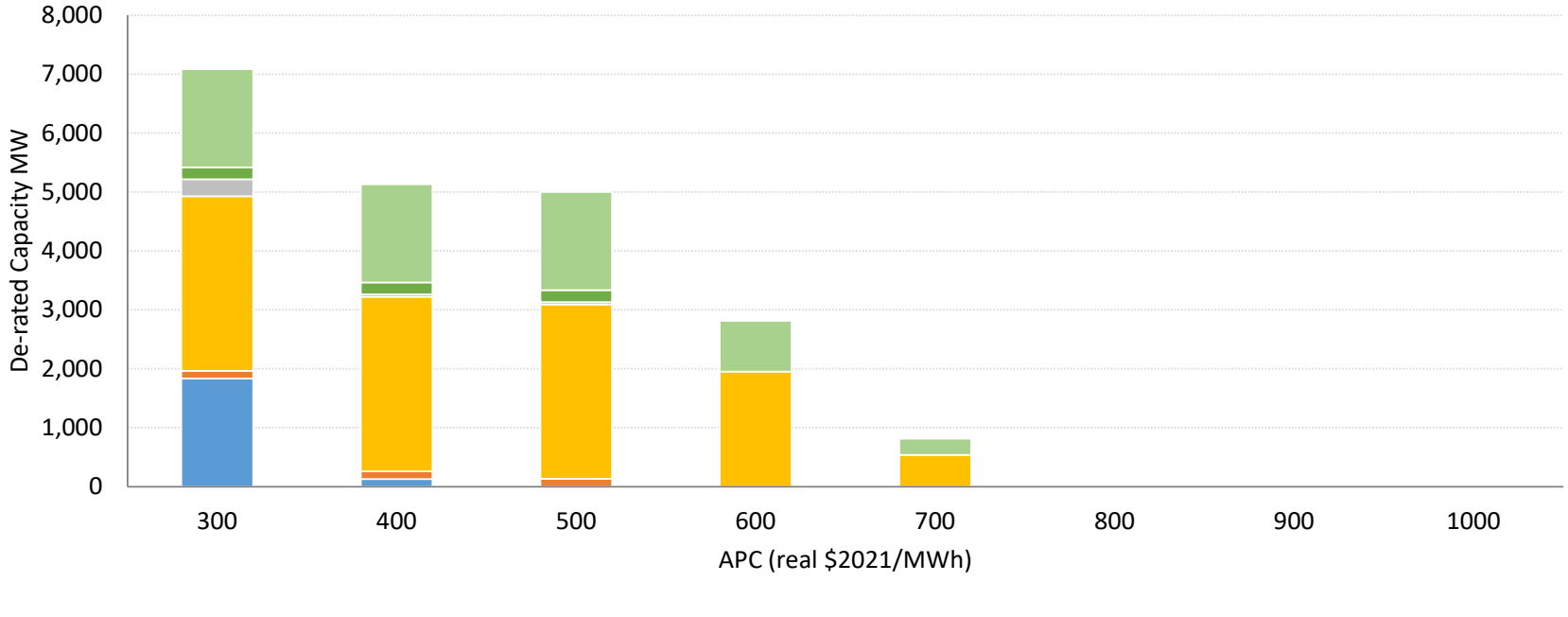
Thermal capacity costs in relation to the APC

- Thermal capacity and heat rates based on AEMO 2022 IASR values
- Gas price of $40/GJ and heat rates from the AEMO 2022 IASR
- Derated MW refers to the average thermal capacity that was available in the period up to the APP in early June



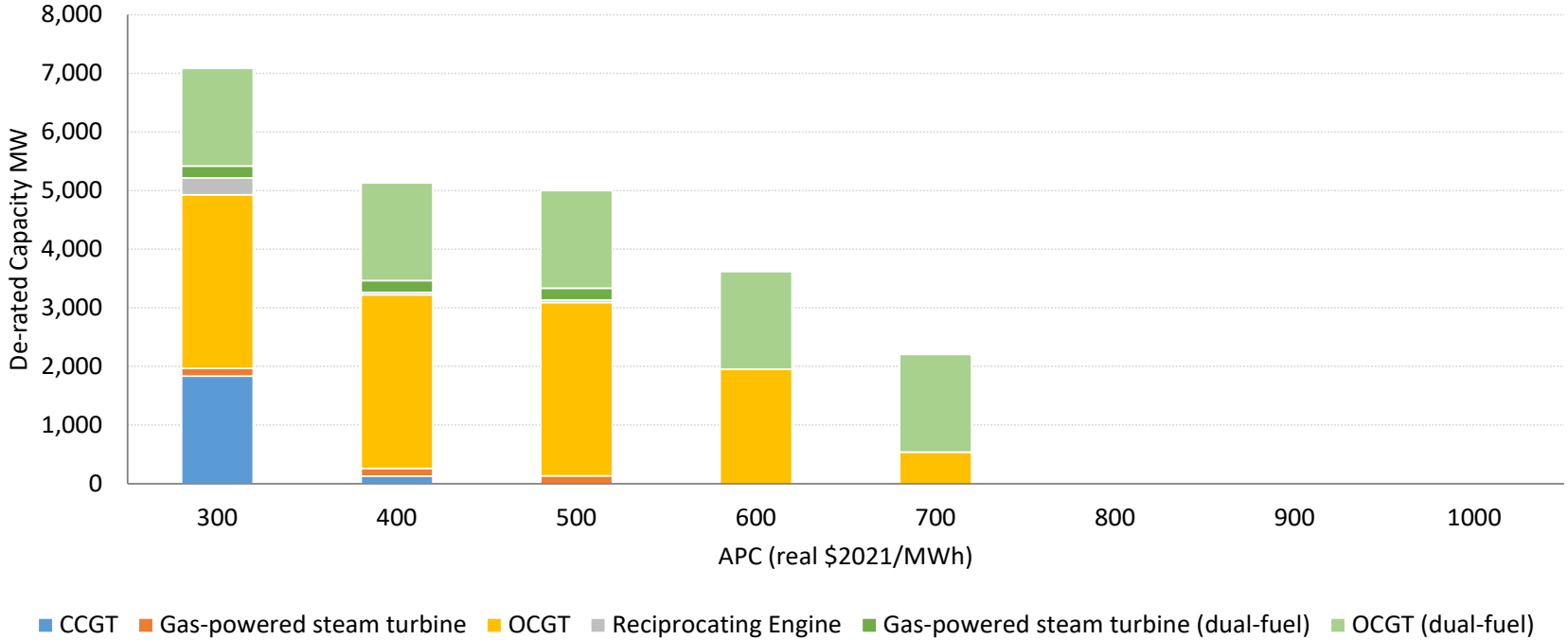
Thermal capacity with SRMC costs exceeding different APC levels

- Calculated using a gas price of $40/GJ and heat rates from the AEMO 2022 IASR



Thermal capacity with SRMC costs exceeding different APC levels - when gas is constrained

- Calculated using gas at $40/GJ, dual fuelled generators using diesel at ~$37/GJ and heat rates from the AEMO 2022 IASR.

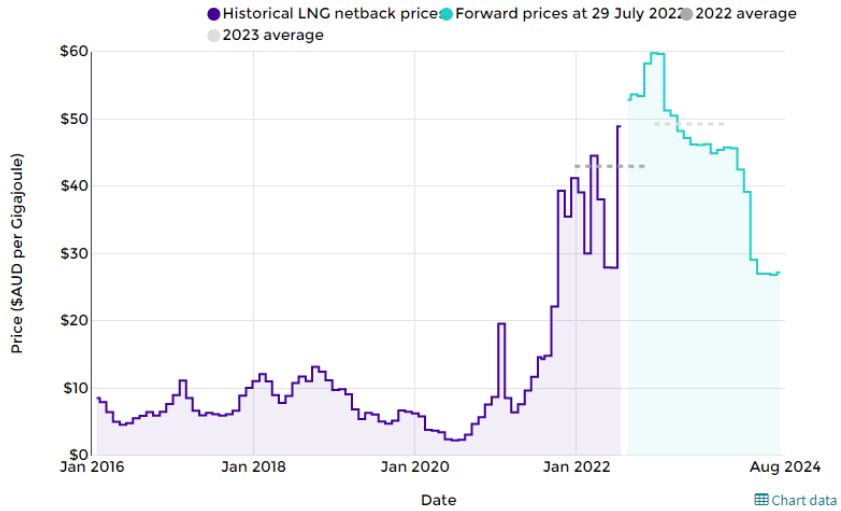


What is an appropriate temporary level of CPT?

- The APC and CPT together act to mitigate the risk of systemic electricity industry collapse during an extreme market event.
- The CPT governs how long high spot prices continue before the APC is applied.
- The risk of systemic collapse relates to market prices and the level of hedging.
    - Greater hedge cover protects a retailer from high spot prices. In the longer term, changes to the CPT could lead to changes in contracting strategies to mitigate new risks.
- High prices during normal market operation lift the cumulative price closer to the CPT - reducing the headroom for market volatility before triggering the APC.
- The interaction between the CPT and APC is a factor to be considered, noting that the CPT is currently calculated with reference to uncapped prices as determined by NEMDE during APP.
- Further analysis is being undertaken on consequent or required temporary changes to the CPT.

Timeframe of application of new levels

- Alinta's rule change proposal suggests that the higher APC should apply for a period of 12 months (or a suitable period as determined by the AEMC with consideration of other processes underway such as the 2022 RSSR).
- The Reliability Panel is considering the level and form of the APC for 1 July 2025 – 30 June 2028.
- Key considerations on timing include:
  - Timing of Reliability Panel recommendations
  - Need for changes to APC to accommodate changing fuel costs faced by generators – what is the expected duration of high commodity prices.
  - Dynamic versus static level
  - Impact on the contract market of different timeframes and changes
  - Alignment of the electricity APC with the gas APC and any potential future changes to gas APC



Last updated on 1 August 2022. Next update on 16 August 2022.

ACCC LNG netback 1 August 2022

QUESTIONS

Questions

- **The problem** – What is the problem the rule change is trying to solve? Does the rule change address the problem? Are there other solutions?
- **Benefits and impacts** – Where the APC and CPT are changed, what is the impact on security and reliability, retailer costs, compensation payments, contract instruments and costs?
- **The APC** – What is an appropriate temporary level? Should there be changes to how the mechanism works?
- **The CPT** – Is there a consequential need to change the CPT? Should the way the CPT is applied or calculated change?
- **Timeframes** – What is an appropriate temporary timeframe? How should this consider RSSR changes, commodity price changes, and contract market needs for stability?

CONCLUDING REMARKS

Key dates for the rule change process

- Key dates:
  - commencement of rule change process: **4 August 2022**,
  - public forum: **16 August 2022**,
  - objections to an expedited process: **18 August 2022**,
  - submissions to the consultation paper: **1 September 2022**, and
  - final decision (expedited process): **29 September 2022**.

  - Reliability settings and standards review final report: 1 September 2022
    - Recommends settings for APC, CPT, MPC, MFP for the period 1 July 2025 to 30 June 2028

AEMC contact details

- **Amending the administered price cap project key contacts:**
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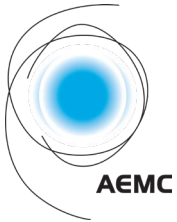
- **Link to project page: https://www.aemc.gov.au/rule-changes/amending-administered-price-cap**

Objections to the expedited process are due on 18 August 2022

Submissions to the consultation paper close on 1 September 2022



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