Mr Craig Oakeshott
Australian Energy Market Commission
Level 6, 201 Elizabeth Street
Sydney NSW 2000

Lodged through online portal

31 August 2022

Dear Ms Oakeshott,

Amending the Administered Price Cap

ENGIE Australia & New Zealand (ENGIE) appreciates the opportunity to respond to the Australian Energy Market Commission ("the Commission") in response to the paper on Amending the Administered Price Cap.

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.

Timing of a potential change

While ENGIE did not oppose the expedited rule change process this should not be taken as a sign ENGIE is not apprehensive about the imposition of rapid change.

In the days prior to the market suspension, putting aside the immense challenge faced by AEMO, the merits of taking emergency action could and perhaps should have been debated before the implementation of a market suspension. However, the suspension has now occurred and the AEMC should not examine the proposal to change the APC through a lens of crisis management but one that supports the long-term interests of customers, and by extension participants and investors.

While ENGIE supports the concept of a change to the APC, all things being equal, this should occur as part of the regular Reliability Standard and Settings Review (RSSR) process such as is already being conducted by the Reliability Panel.

Notably, few, if any, submissions to the RSSR advocated an increase to the APC prior to the market suspension.

Is a change to the APC the preferred method?

While the rule change proposal focuses on the APC, it is correct that alternative options exist.

ENGIE has long advocated a decoupling of the CPT from the MPC on the basis they serve two quite distinct purposes, and each has outgrown the basic formulaic determination of the CPT from the MPC.

ENGIE has previously suggested that the CPT should be calculated based on the ability of the market to withstand high prices without creating a significant risk of cascading default. This was raised by other participants in the NEM Financial Resilience review (including Alinta Energy) but after a decade few policy makers have been minded to investigate such a change.

Nonetheless, when considered in the context of the challenges presented by the APC during June, there is a case to be made that the financial risks created by suspending the market exceeded the financial risks that would have arisen if the CPT was higher. Going further, if the CPT was higher, then it may have been the case that the APC would not have worked with the CPT to keep the market in APC for an extended period which only ceased with market suspension.

On this basis, an emergency change on a temporary basis may be better targeted at the CPT and not the APC. If this was the preferred approach, then the AEMC would need to identify the trade-offs between higher CPT's and risks to market participants under "normal" and extreme conditions like those experienced in June.

While this may sound challenging, the counter-factual, a temporary change to the APC, is likely to have a more significant and unmanageable impact on participants and contract markets.

Temporary solutions are less desirable

While the urgency to support a temporary solution was understandable in early June, the case now is less compelling and therefore it may be desirable to change the APC based on a long-term methodology that participants can have confidence in.

Upon reflection since June, ENGIE has growing concerns that making a temporary change, and making a change rapidly, may set a poor precedent and undermine the confidence with which participants hold the RSSR process.

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

AEMC

Amending the administered price cap rule change

STAKEHOLDER FEEDBACK TEMPLATE

The template below has been developed to enable stakeholders to provide their feedback on the questions posed in the consultation paper and any other issues that they would like to provide feedback on. The AEMC encourages stakeholders to use this template to assist it to consider the views expressed by stakeholders on each issue. Stakeholders should not feel obliged to answer each question, but rather address those issues of particular interest or concern. Further context for the questions can be found in the consultation paper.

SUBMITTER DETAILS

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DATE	1 September 2022

PROJECT DETAILS

NAME OF RULE CHANGE:	**Amending the administered price cap**
PROJECT CODE:	**ERC0347**
PROPONENT:	**Alinta Energy**
SUBMISSION DUE DATE:	**1 September 2022**

CHAPTER 4 – ASSESSMENT CRITERIA

a. Is the proposed assessment framework appropriate for considering the proponent's rule change request?	Yes, broadly speaking.
b. Are there any other relevant considerations that should be included in the assessment framework?	The criteria appear sufficient for the purposes of considering the merits of the rule change proposal or its alternatives..

CHAPTER 6 – ISSUES FOR CONSULTATION: PROBLEM STATEMENT

1. Has the problem been appropriately identified? For example, is the current level of the APC, owing to the recently increased cost of generation, the principal problem or a key contributing factor?	Yes, the problem has been appropriately identified. Whether the current level of the APC is the principal problem *or* a key contributing factor is not especially relevant - it is certainly one of the two, but reasonable people may differ on what is the principal problem. For example, AEMO has stated in respect of the APC and market suspension period that: "The confluence of high commodity prices, domestic gas market and subsequently NEM price caps, planned and unplanned outages of scheduled generating plant, low output from semi-scheduled generation, and high winter demand conditions led to unprecedented challenges operating the NEM" [1].So any one of these factors could be identified as the principal problem. But, in general, they are all external factors that cannot be straightforwardly addressed by changes in the energy rules. By contrast, the APC is an artefact of the rules, a deliberate market distortion. It can be changed because it played a major role in the recent market dysfunction, whether it should, is the subject of this rule change.
2. Is there a risk that a failure to address the problem identified would have a significant negative economic impact and be inconsistent with the long-term interests of consumers?	All scenarios present a risk to the long-term interests of customers, and it is not possible to say with confidence a change should or should not occur given future events remain uncertain. It is known that given everything that occurred in the lead-up to the progressive application of the APC across the NEM in June, and the extant issues during the periods of APC (i.e., prevailing fuel costs, energy scarcity, unplanned outages, etc.), it's clear that the APC was too low to allow the market to effectively clear. The problem was not confined to high SRMC plant such as gas and diesel peakers. Energy-limited plant, including hydro, coal (due to severe issues with coal delivery) and battery storage did not have sufficient visibility of the periods of maximum scarcity (which in normal market operation would be signalled by high prices approaching or at the MPC) to determine when to run. Nor did they have confidence that they could structure their bidding appropriately to be able to effectively ration their limited energy for the periods of greatest need. Accordingly, as AEMO noted: "The application of the APC…coincided with reductions in the volume of generation offered to the market." This in turn resulted in deterioration in the quality of information in ST-PASA, an excessive issuance of LOR notices and other signs of market dysfunction. Perhaps most critically, the "physical run" prices were stuck at the MPC due to the limited volume of generation still able to participate in the market, perpetuating the application of the APC as cumulative prices remained above the CPT. In these circumstances, market suspension may have been inevitable. Even then, there were risks to power security arising from the complexities of manual dispatch. But it did at least serve as a circuit breaker for the CPT to fall below the threshold and allow normal market operations to be resumed.

[1] AEMO, *NEM market suspension and operational challenges in June 2022*, August 2022, p5

3. Does the rule change address the problem?	Potentially, subject to the views expressed below re the optimal level of the APC and the duration of the revised level. Broadly, though, a significant increase in the APC to better reflect the contemporary SRMC of the marginal generator in the NEM would address the problem that the current level of the APC is too low. The concern for ENGIE is whether this should be temporary, whether emergency changes are desirable, and if so, are there better alternatives to a change in the APC on a temporary basis outside the RSSR cycle?
4. Is the rule change the best solution to the problem? Are there other solutions that would better solve the problem over the timeframe considered?	ENGIE is leaning to the view that a increase in the CPT would be less risky and better deal with the issues at hand. Although both options require further analysis.

CHAPTER 6 – ISSUES FOR CONSULTATION: PROPOSED SOLUTION

5. Is Alinta's proposed amendment to the APC rule appropriate to address the problem?	ENGIE is leaning to the view that a increase in the CPT would be less risky and better deal with the issues at hand. Although both options require further analysis.
6. Given current commodity prices, what level of APC is appropriate to enable the normal market operation and settlement under an APP?	ENGIE's view is that the APC should reflect the SRMC of the marginal generator. The analysis the Commission has presented in the Consultation Paper indicates this could be in the order of $800/MWh. ENGIE considers that the risks and consequences of the market getting stuck in APC or even a repeat of market suspension are sufficiently serious that in setting the APC (i.e., by making a more preferable rule), the AEMC should err on the high side.

7. What is the impact of such a change likely to be on generator and retailer risks borne in participating in the market?	Any change requires a sufficiently long lead time, and this analysis presumes such. Without such a lead time the risks would be significantly greater. Generators will be less likely to be exposed to the risks entailed in an APC situation, such as an inability to recover SRMC (except via lengthy and uncertain compensation application processes) or an inability to effectively ration limited energy supplies. Conversely, they will have to consider the risks that any contract position exposes them to prices between $300 and the new APC during an APC period in the event that they cannot physically defend their contract position (e.g., due to energy limitations or unplanned outages). Retailers will be less likely to be exposed to unhedgeable costs such as RERT costs and the various forms of compensation arising from APC/market suspension events. Providing prices mostly clear under a new, higher APC, as they should, if set at an appropriate level, they may on average exceed $300/MWh, but they will be hedgeable, meaning retailers need not be exposed, and given the rarity of APC events, the incremental hedging cost is unlikely to be significantly higher. In the short term, retailers will have to consider how to adjust their existing contract position in the light of the risks that their existing contract position exposes them to prices between $300 and the new APC during an APC period. Given both the supply and demand side would benefit from access to hedging tools targeted at the new APC level, the Commission should be confident that the market will find ways to create these. ENGIE notes that the extent of retailers' exposure will depend on their customer base and whether retail contracts allow them to pass through unhedgeable costs. While this will not be the case for small customers, it may well be for commercial and industrial customers. In this instance, those customers will benefit from a higher APC to the extent that they can then manage price risk through their retail contract and will be less likely to face unhedgeable costs being passed through.
8. How might the APC change to accommodate different commodity price assumptions?	The APC could be set on a formula based on the maximum expected fuel price multiplied by the likely heat rate of the relevant generation type. The relevant commodity price could be a natural gas price – which would be capped by gas price caps in facilitated markets plus a reasonable transport cost allowance. However, a more flexible approach would be to recognise more than one commodity/generation type and set the APC on the higher/highest of them. ENGIE notes that the calculation in the consultation paper of a 99th percentile diesel fuel cost could serve as a maximum price for commodities that aren't subject to a facilitated market price cap. Renewable hydrogen may also be a relevant commodity for this purpose in the future.

9. What are alternative options for amending the level of APC. Options could include, for example, different levels of APC for different technologies, different values in each region, values that change by time of day, linkages between the electricity APC and the gas APC?	ENGIE supports dynamic APC levels, that can automatically change periodically if maximum underlying fuel prices change. However, granular APCs for different technologies, regions and time of day seem unduly complex and risk introducing distortions into the market. For an emergency change, ENGIE favours the AEMC analysing the merits of changing the CPT.

CHAPTER 6 – ISSUES FOR CONSULTATION: TEMPORARY LEVEL OF THE CPT

10. Is there any consequential need for a change to the CPT resulting from a temporary change to the level of APC?	As the Consultation Paper notes, the current CPT equates to an average of $674/MWh across a week. This may potentially be lower than the revised MPC based on the criteria ENGIE has proposed above. A situation where the APC exceeds the seven-day average price needed to reach the CPT risks market dysfunction where a region (or the NEM as a whole) cannot get out of the APC because the APC does not function to bring cumulative prices below the CPT. Accordingly, the CPT must be set at a level such that the seven-day average price needed to reach the CPT is higher than the APC (it need not be much lower). This is consistent with ENGIE's view that it is timely to decouple the CPT from the MPC and the CPT should exist primarily to reduce the risk of cascading default.
11. Should the calculation of the CPT be different during the APP?	The only alternative approach to that set out above would be to apply an alternative, higher CPT generally, during periods of APC as an emergency measure. This would be useful in the case of a dynamic APC, where the CPT could be set at: (applicable APC + $x/MWh) x 2,016.
12. Is there a more appropriate method of triggering the APC?	Unclear at this time.
13. Should a temporary change to the level of the APC consider the interaction between the gas APC and electricity APC?	Yes, as discussed above, ENGIE considers a good benchmark for the APC is to reference relevant commodity costs and heat rates to derive an APC that reflects the maximum SRMC in the NEM.

CHAPTER 6 – ISSUES FOR CONSULTATION: TIMEFRAME OF APPLICATION OF PROPOSED RULE

14. What is an appropriate temporary timeframe for application? Considering the factors that require the rule change to be made including commodity price changes?	ENGIE appreciates the intent of the proposed sunset period is to reflect that this is an urgent rule change and that a longer-term change to the APC would benefit from a full consultation process rather than an expedited one, as well as to take account of any relevant recommendations from the Reliability Panel. However, either the Panel will recommend a change to the APC (and potentially the CPT), in which case there is likely to be another rule change on the subject shortly, which will supersede this one, or they will recommend no change. Thus a timeframe for change ahead of the RSSR process sis only justifiable if the risks to the market are so great that participants should be exposed to expedited and unexpected changes.
15. What consideration should be made of changes and the timing of changes to be introduced by the Reliability Panel?	The Reliability Panel is due to publish its final Reliability Standard and Settings Review on the same day that submissions are due to this consultation. Accordingly, stakeholders have no way to know what the Reliability Panel will recommend. At a minimum, this rule change should not proceed if the Reliability Panel charts an alternative pathway forward.
16. How should a temporary change in the level of APC accommodate changes to commodity prices during its application?	ENGIE is not convinced of a temporary change.
17. What are the consequences for the retail and contract markets from one-off or sequential changes to APC?	Contract markets are more likely to respond effectively to a longer-term change in the APC than a temporary 12 month change. Introducing new contracts, especially standardised exchange traded contracts, has some cost and takes some time to implement. So, there may be barriers to the introduction of appropriate new contracts if there is only a short-term change.
18. Should there be a mechanism to ensure that the APC is dynamic and indexed with an appropriate commodity price?	Potentially, but how this change can be managed requires further analysis.

CHAPTER 6 – ISSUES FOR CONSULTATION: BENEFITS AND IMPACTS

Security and reliability

19. What is the likely impact of a temporary change in APC on security and reliability through APP periods and through the avoidance of market suspension? What would be the likely impact of a temporary change in the CPT?	ENGIE considers that the recent market suspension resulted in risks to security and threatened reliability, albeit no forced load shedding was in the end required. This is documented in AEMO's report into the suspension period[2]. Reducing the risk of market suspension would enhance security and reliability compared to the status quo. This can be done via a change to the CPT, APC or possibly other.

[2] Ibid

Cost of Energy

20. Would a temporary change to the level of APC likely reduce costs to market participants over the timeframe applied? Should temporary changes to the level of CTP be considered?	See response to question 22 below.
21. Would a temporary change to the level of APC likely reduce costs to market participants over the timeframe applied? Should temporary changes to the level of CTP be considered?	See response to question 22 below.
22. Would a change to APC increase or reduce the wholesale cost of energy during APP periods? Should a change to the CPT be considered?	It's unclear whether the eventual cost (including compensation) of wholesale energy would be higher or lower if the APC or CPT is increased. Importantly, though, it is likely to be easier to hedge against these costs if the APC or CPT is higher, because a smaller proportion of wholesale costs will be unhedgeable compensation costs.

Contract market and financial requirements

23. What is the likely impact of a temporary change in the level of APC on ASX exchange traded contracts, OTC contracts and any other electricity contract products. In relation to existing contract clauses, the effectiveness of these products in addressing retailer risk, and the value of fixed price contract instruments? What would be the impact of a change to the CPT?	Depending on the change, some contracted parties would be significantly affected by a change and their contracting behaviour would reflect this.
24. What is the likely impact of a temporary change in APC on retailer credit support requirements? What would be the likely impact of a temporary change in the CPT?	To the extent that a change (temporary or otherwise) in the APC or CPT results in higher contract prices, then it could result in an increase in credit support requirements and other prudentials. However, as the Consultation paper notes, these may already have increased materially due to the recent extended period of elevated prices. So, the overall impact on the market is not expected to be significant.
25. What is the likely impact of a temporary change in APC on NEM bank guarantees and security deposits to support trading? What would be the likely impact of a temporary change in the CPT?	See response to question 24 above.
26. What costs are imposed by the imposition of a temporary	As discussed above, developing new contract types (or new clauses in existing standard clauses) takes time and has costs.

change, on a market setting that is normally unchanging?	If the short-term nature of the change inhibits appropriate development of new contracts, then this will be reflected in increased risks to participants unable to access contracts that assist them in managing against the new APC level.