



# RULE CHANGE

Australian Energy Market Commission

## RULE DETERMINATION

### National Electricity Amendment (Application and Operation of Administered Price Periods) Rule 2011

#### **Rule Proponent(s)**

Australian Energy Market Operator

#### **Commissioners**

Pierce  
Henderson  
Spalding

10 November 2011

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## **Citation**

AEMC 2011, Application and Operation of Administered Price Periods, Rule Determination, 10 November 2011 , Sydney

## **About the AEMC**

The Council of Australian Governments, through its Ministerial Council on Energy (MCE), established the Australian Energy Market Commission (AEMC) in July 2005. The AEMC has two principal functions. We make and amend the national electricity and gas rules, and we conduct independent reviews of the energy markets for the MCE.

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## Summary

On 21 July 2011 the Australian Energy Market Commission (AEMC, Commission) published its draft Determination regarding the rule change request submitted by the Australian Energy Market Operator Limited (AEMO, proponent) relating to the application and operation of administered price periods in the National Electricity Market (NEM)<sup>1</sup>.

In this Final Determination, the Commission has decided to implement all the proposed decisions in the draft Determination as well as those proposed in the further consultation paper released on 22 September 2011<sup>2</sup>. These include amendments to :

- make it clear that an Administered Price Period (APP) for Market Ancillary Services (MAS) commences at the dispatch interval following the dispatch interval in which a cumulative ancillary service price exceeds six times the Cumulative Price Threshold (CPT);
- clarify that all MAS prices are limited to the Administered Price Cap (APC) where an APP is notified for energy or any MAS;
- remove AEMO's discretion to extend an APP to the next trading day when the CPT is no longer breached;
- allow AEMO up to 25 business days to fulfill its obligations to include compensation awarded by the AEMC; and
- modify the calculation of price constraints in neighbouring regions under the application of the APC, Administered Floor Price (AFP), Market Price Cap (MPC), Market Floor Price (MFP), and during market suspension of a region.

Three submissions were received to the draft Determination, from the Australian Energy Regulator (AER), National Generators Forum (NGF), and AEMO.

The respondents either supported or did not comment on aspects of the Draft Rule as described in the draft Determination, with the following exceptions:

- The AER disagreed that the extension of APPs ahead of time should be removed, arguing for the use of forecast prices to automatically determine whether the APP should be continued;
- The NGF disagreed that the eight MAS prices should be capped to the APC during an APP triggered by a particular MAS, arguing that Raise and Lower<sup>3</sup> services should be capped independently;

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<http://www.aemc.gov.au/Media/docs/Draft%20Determination-fb9cdc60-d7a7-4452-ab08-c9db9cee5bd6-0.PDF>

- The NGF disagreed with the assertion that the combined effects of AEMO's powers of direction and the compensation arrangements were sufficient to address the potential incentive generators would have to withdraw from Raise services during an APP. The NGF prefer the use of a more explicit solution such as one whereby MAS prices would be capped to either the APC or the energy dispatch price, whichever was higher;
- AEMO proposed that the clauses which constrain prices in neighbouring regions during periods of interventionary pricing (including market suspension) be amended in relation to their use of loss factor adjustments. The Commission saw merit in the proposal but noted that it covered clauses and content not previously consulted on, so it published a further paper on this topic on 23 September 2011.

The Commission considered the submissions on the draft Determination and, having considered all potential options and the costs of potential changes, has decided to confirm all the decisions put forward in its draft Determination. Having received no response to the further consultation, the Commission has further decided to implement as-drafted the proposals laid out in that paper. The rule as made takes effect from 10 November 2011, with exception of the amendments to the clauses which constrain prices in neighbouring regions during periods of interventionary pricing (including market suspension). These are instead to take effect from 2 July 2012.

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<http://www.aemc.gov.au/Media/docs/Further%20Consultation%20Paper-53b3b41b-be33-484c-b05f-831f8c9e2bf7-0.PDF>

3

'Raise' services here refer to the four ancillary services that when called upon, act to increase the system frequency. 'Lower' refers to the four services that lower the system frequency.

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# 1 AEMO's Rule Change Request

## 1.1 The Rule Change Request

On 4 January 2011, the AEMO made a request to the Commission to make a rule regarding the application and operation of administered price periods (rule change request).

The rule change request sought to clarify the meaning of the clauses relating to APPs in the National Electricity Rules (NER), and proposed an extension to the timeframe in which AEMO is required to include compensation payable due to the application of an APP, MPC or MFP in participants' preliminary and final statements.

## 1.2 Rationale for the Rule Change Request

In the rule change request the rule proponent contended that:

- It was necessary to improve the clarity of the rules relating to the application and operation of APPs, including:
  - clarifying that an APP triggered by MAS would commence in the dispatch interval that immediately follows the dispatch interval in which the sum of an ancillary service price for the previous 2016 dispatch intervals exceeds six times the CPT;
  - removing ambiguity in clauses 3.14.2(d1) and 3.14.2(d2) of the rules to clarify that all MAS prices are capped at the APC during an APP triggered by any single MAS.
- The process for the discretionary extension of an APP to the next trading day was of limited and questionable benefit to the market, as its use would require subjective decision making on the part of AEMO / AER that is not guided by the NER. This could create unnecessary market uncertainty and inconsistent outcomes.
- AEMO currently do not have sufficient time to reasonably settle compensation amounts relating to the imposition of an APC, MPC or MFP.
- Clause 9.45.2 of the Rules, relating to the Tasmanian Region, was redundant given the application of an updated APC to all regions, which occurred in 2008.
- Various references to "market ancillary service price" were misleading as they unnecessarily combine two Glossary definitions.

### 1.3 Solution proposed in the Rule Change Request

The rule proponent proposed to resolve the issues discussed above by making a Rule that sought to:

- clarify clause 3.14.2(c)(1A) to make it clear that an APP triggered by MAS commences in the dispatch interval that immediately follows the dispatch interval in which the sum of an ancillary service price for the previous 2016 dispatch intervals exceeds six times the CPT;
- clarify that clause 3.14.2(d2) requires AEMO to limit all MAS prices to the APC where an APP is notified for energy or any MAS;
- delete clause 3.14.2(c)(3) which allows AEMO to impose an APP for the next trading day based on its opinion of the likelihood of another APP being applied in a trading interval on that day, or amend the drafting to remove ambiguity relating to how AEMO would decide to exercise such a discretionary function;
- amend clause 3.15.10(c) to allow AEMO up to 25 business days to fulfill its obligations to include compensation awarded by the AEMC under clause 3.14.6 in statements provided under clauses 3.15.14 and 3.15.15;
- include a reference to the term 'dispatch prices' in 3.14.1(a), and employ a transitional provision that would direct the AEMC to make an amendment to the Administered Price Cap schedule without following the Rules consultation procedures (given the matter is a minor clarification only);
- omit "market" and italicise the term "ancillary service prices" wherever occurring in clauses 3.14.1(a), 3.8.24(b), 3.9.2A(d), 3.13.7(e)(3) and (4), 3.14.1(a) and 3.15.7(c);
- omit "market ancillary services prices" and substitute with "ancillary service prices" italicised in clause 3.9.2B(e)(1);
- delete clause 9.45.2, which explicitly stipulated the value of the APC in Tasmania prior to the establishment of the existing APC of \$300/Megawatt-hour (MWh) which now applies to all regions.

### 1.4 Commencement of Rule making process

On 31 March 2011, the Commission published a notice under section 95 of the National Electricity Law (NEL) advising of its intention to commence the rule change process and the first round of consultation in respect of the rule change request. A consultation paper prepared by AEMC staff identifying specific issues or questions for consultation was also published with the rule change request. Submissions closed on 12 May 2011.

The Commission received three submissions to the rule change request as part of the first round of consultation. They are available on the AEMC website<sup>4</sup>. A summary of the issues raised in submissions and the Commission's response to each issue, published in its draft Determination, is contained in Appendix A.1.

## 1.5 Publication of draft Rule Determination and Draft Rule

On 21 July 2011 the Commission published a notice under section 99 of the NEL and a draft Rule determination in relation to the rule change request (Draft Rule Determination). The Draft Rule Determination included a draft Rule (Draft Rule).

Submissions on the Draft Rule Determination closed on 1 September 2011. The Commission received three submissions on the Draft Rule Determination. They are available on the AEMC website<sup>5</sup>. A summary of the issues raised in submissions, and the Commission's response to each issue, is contained in Appendix A.2.

## 1.6 Further Consultation

On 22 September 2011 the Commission published a notice under section 107A of the NEL to extend the publication date of the final Rule determination by four weeks to 10 November 2011 to allow for further consultation<sup>6</sup> on issues raised by AEMO that proposed to make various minor amendments to the rules in relation to the application of average loss factors in the APP, MPC and MFP clauses. This consultation is termed the 'further' consultation in this document to distinguish it from the first<sup>7</sup> and second<sup>8</sup> rounds.

The Commission received no submissions on the further consultation.

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4 [www.aemc.gov.au](http://www.aemc.gov.au)

5 [www.aemc.gov.au](http://www.aemc.gov.au)

6 <http://www.aemc.gov.au/Media/docs/Notice%20of%20S107A%20-%2022%20September%202011-7d59295e-1c36-4ff4-9d55-a1f9a6791408-0.pdf>

7 <http://www.aemc.gov.au/Media/docs/Consultation%20Paper-df191051-c600-4042-97b0-d2f517e3ce27-0.PDF>

8 <http://www.aemc.gov.au/Media/docs/Draft%20Determination-fb9cdc60-d7a7-4452-ab08-c9db9cee5bd6-0.PDF>

## **2 Final Rule Determination**

### **2.1 Commission's determination**

In accordance with section 102 of the NEL the Commission has made this final Rule determination in relation to the Rule proposed by AEMO. In accordance with section 103 of the NEL the Commission has determined to make, with amendments, the rule proposed by the rule proponent<sup>9</sup>.

The Commission's reasons for making this final Rule determination are set out in section 3.1.

The *National Electricity Amendment (Application and Operation of Administered Price Periods) Rule 2011 No [9]* (Rule as Made) is published with this final Rule determination. The Rule as Made commences on 10 November 2011. The Rule as Made is different from the Rule proposed by the rule proponent. Its key features are described in section 3.2.

### **2.2 Commission's considerations**

In assessing the rule change request the Commission considered:

- the Commission's powers under the NEL to make the Rule;
- the rule change request;
- the fact that there is no relevant Ministerial Council on Energy (MCE) Statement of Policy Principles<sup>10</sup>;
- submissions received during the first and second rounds of consultation<sup>11</sup> ; and
- the Commission's analysis as to the ways in which the proposed Rule will or is likely to, contribute to the achievement of the National Electricity Objective (NEO).

### **2.3 Commission's power to make the Rule**

The Commission is satisfied that the Rule as Made falls within the subject matter about which the Commission may make Rules. The Rule as Made falls within the matters set

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<sup>9</sup> Under section 103(3) of the NEL the Rule that is made in accordance with section 103(1) need not be the same as the draft of the purposed Rule to which a notice under section 95 relates or the draft of a Rule contained in a draft Rule determination.

<sup>10</sup> Under section 33 of the NEL the AEMC must have regard to any relevant MCE statement of policy principles in making a Rule.

<sup>11</sup> No submissions were received to the further consultation under section 107A

out in section 34(1)(a)(i) of the NEL as it relates to regulating the operation of the National Electricity Market.

## 2.4 Rule making test

Under section 88(1) of the NEL the Commission may only make a Rule if it is satisfied that the Rule will, or is likely to, contribute to the achievement of the NEO. This is the decision making framework that the Commission must apply.

The NEO is set out in section 7 of the NEL as follows:

“The objective of this Law is to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to:

- (a) price, quality, safety, reliability and security of supply of electricity;  
and
- (b) the reliability, safety and security of the national electricity system.”

For the rule change request, the Commission considers that the relevant aspects of the NEO<sup>12</sup> include the promotion of efficient investment in, and efficient operation of, electricity services for the long term interests of consumers of electricity with respect to price. This is because the application and operation of administered price periods directly affects dispatch prices which influence the final price paid by consumers. Other relevant aspects of the NEO include security of supply and security of the national electricity system, as administered price periods tend to co-incide with periods of system stress, so their application and operation could impact on the market signals that are sent to providers of electricity and providers of system support services during such periods.

The Commission is satisfied that the Rule as Made will, or is likely to, contribute to the achievement of the NEO because it improves transparency of the market arrangements and provides greater certainty for participants and AEMO. This will, all else equal, reduce barriers to investment, facilitating competition and thereby lowering the long-term price of electricity, for the long-term interest of consumers.

Under section 91(8) of the NEL the Commission may only make a Rule that has effect with respect to an adoptive jurisdiction if satisfied that the proposed Rule is compatible with the proper performance of AEMO’s declared network functions. The Draft Rule is compatible with AEMO’s declared network functions because it does not interfere with, or in any way impact upon, AEMO’s ability to perform its declared network functions.

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<sup>12</sup> Under section 88(2), for the purposes of section 88(1) the AEMC may give such weight to any aspect of the NEO as it considers appropriate in all the circumstances, having regard to any relevant MCE statement of policy principles.

## **2.5 Implementation**

The rule as made takes effect from 10 November 2011, with the exception of the amendments to clauses 3.9.5(c), 3.9.6A(c), 3.14.2(e)(2), 3.14.2(e)(4) and 3.14.5(m) which are to take effect from 2 July 2012. The amendments to these five clauses are to take effect at the later date because AEMO will be required to make changes to the Electricity Market Management Systems.

### 3 Commission's reasons

The Commission has analysed the rule change request and assessed the issues/propositions arising out of this rule change request. For the reasons set out below, the Commission has determined that a Rule should be made. Its analysis of the Rule proposed by the rule proponent is also set out below.

#### 3.1 Assessment

The rule change request seeks to clarify the application and operation of APPs in the NEM, and remove AEMO's discretion to extend an APP once triggered.

In addition to the issues raised in the rule change request, the following issues were identified following receipt of first and second round submissions:

- An unwanted incentive to withdraw market ancillary services could potentially arise under the current APP arrangements when an APP is triggered by market ancillary services.
- Drafting errors appear to exist in clauses 3.14.2(e)(4) and 3.9.6A(c) that should be corrected.
- Clarifications should be made to clauses 3.9.5(c), 3.9.6A(c), 3.14.2(e)(2), 3.14.2(e)(4) and 3.14.5(m) with regard to the directional reference of loss factor adjustments.

Following analysis and consideration of submissions to the first and second round of consultation, the Commission has determined consistent with its draft Determination that removing AEMO's discretion to extend an APP to the next trading day would best contribute to the achievement of the NEO, compared to other options considered. This approach is preferred to the option of introducing an objective test for the extension of an APP suggested as an alternative by AEMO, or the option of confirming the subjective opinion-based approach presently in the Rules.

The Commission considers that no material risks would emerge by commencing an APP in the dispatch interval immediately following the dispatch interval in which an APP is triggered by the sum of ancillary service prices exceeding six times the Cumulative Price Threshold. Further the Commission considers that this arrangement is the most compatible with the objective of efficiency, in that the intervention in price setting is applied as close as possible to the instance in which the relevant conditions for doing so are triggered.

The Commission has determined consistent with its draft Determination that for APPs triggered by a high ancillary service price, it should be clarified that all ancillary service prices should be capped at the APC<sup>13</sup>. No such cap would be applied to the

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<sup>13</sup> The AEMC's draft Determination erroneously made reference to corresponding flooring of ancillary service prices to the AFP as part of its decision. Ancillary service prices in fact can not be

dispatch price, however, for the same reasons laid out by the Australian Competition and Consumer Commission (ACCC) in their Determination relating to Regional Pricing of Ancillary Services of September 2003<sup>14</sup>; in which the ACCC stated “...the benefits in having an APC in the energy market as a result of high prices in one of the FCAS markets is not clear given that the volumes in the FCAS markets are small relative to those in the energy market.”

The Commission notes that no respondents raised any material concerns with the proposed extension of the time allowed for AEMO to fulfill its obligations to include compensation awarded by the AEMC under clause 3.14.6 in statements provided under clauses 3.15.14 and 3.15.15. The Commission is consequently satisfied that the proposal to extend the time allowed is reasonable and has determined consistent with its draft Determination on this matter.

The Commission considers that clauses 3.14.2(e)(4) referring to application of the AFP, and 3.9.6A(c) referring to application of the MFP, should be amended to refer to flows away from, rather than toward the region affected by manual price setting and has determined consistent with its draft Determination on this matter.

The Commission also has decided that the clarifications regarding loss factor applications in clauses 3.9.5(c), 3.9.6A(c), 3.14.2(e)(2) and 3.14.2(e)(4) proposed by AEMO in their response to the draft Determination be implemented as put forward in the further consultation paper, along with a corresponding amendment to clause 3.14.5(m), also laid out in the further consultation paper.

## **3.2 Rule as Made**

The Commission has determined to make the Rule as Made to:

- amend clause 3.14.2(c)(1A) to make it clear that an APP for MAS commences at the dispatch interval following the dispatch interval in which a cumulative ancillary service price exceeds six times the CPT;
- clarify that clause 3.14.2(d2) requires AEMO to limit all MAS prices to the APC where an APP is notified for energy or any MAS;
- delete clause 3.14.2(c)(3), which grants AEMO discretion to extend an APP to the next trading day when the CPT is no longer breached;
- amend clause 3.15.10(c) to allow AEMO up to 25 business days to fulfill its obligations to include compensation awarded by the AEMC under clause 3.14.6 in statements provided under clauses 3.15.14 and 3.15.15;

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less than zero as laid out in clause 3.9.2A(c), and this rule determination does not affect or alter that arrangement.

<sup>14</sup> Determination 'Applications for Authorisation: Amendments to the National Electricity Code - Regional Pricing of Ancillary Services' 17 September 2003, p16.

- include a reference to the term 'dispatch prices' in 3.14.1(a), and employ a transitional provision to give this effect in the APC Schedule;
- omit "market" and italicise the term "ancillary service prices" wherever occurring in clauses 3.14.1(a), 3.8.24(b), 3.9.2A(d), 3.13.7(e)(3) and (4), 3.14.1(a) and 3.15.7(c);
- omit "market ancillary services prices" and substitute with "ancillary service prices" italicised in clause 3.9.2B(e)(1);
- delete clause 9.45.2, which explicitly stipulated the value of the APC in Tasmania which is no longer required;
- amend clauses 3.9.6A(c) and 3.14.2(e)(4) to:
  - refer to flows "away from" instead of "toward" the regional reference node at which the dispatch price is set to the market / administered floor price;
  - delete "product of the"; and
  - replace references to flow "between" the nodes to specify the direction of flow that the reference applies to.
- amend clauses 3.9.5(c), 3.14.2(e)(2) and 3.14.5(m) to:
  - delete reference to "multiplied by" the loss factor and replace with "divided by";
  - delete "product of the" in clauses 3.9.5(c) and 3.14.2(e)(2); and
  - replace references to flow "between" the nodes to specify the direction of flow that the reference applies to.

### 3.3 Civil Penalties

The Rule as Made does not amend any Rules that are currently classified as civil penalty provisions under the *National Electricity Law* or *Regulations*. The Commission does not propose to recommend to the MCE that any of the provisions amended by the Rule as Made be classified as civil penalty provisions.

## 4 Commission's assessment approach

This chapter describes the Commission's approach to assessing the rule change request in accordance with the requirements set out in the NEL (and explained in Chapter 2).

### 4.1 Issues

In assessing the rule change request, the Commission has considered the following issues:

- Discretion (clause 3.14.2(c)(3))
  - The current discretion that AEMO has to extend an APP to the next day.
  - The potential alternative arrangements, including:
    - 1 Removing the discretion by deleting the clause as proposed by the proponent.
    - 2 Obligating AEMO to develop an objective test for the extension of an APP to the next trading day.
    - 3 Creating an objective test that could be written into the Rules.

In each arrangement, the role played by AER could also be:

- confirmed as currently drafted.
- Removed as proposed by the rule proponent.
- Modified.
- Dependency of APC Applications to MAS prices (clauses 3.14.2(d)(1) and (2))
  - Retention of the current drafting relating to dependencies of applications of the APC to MAS prices.
  - Clarification of the meaning and rewording of the existing clauses.
  - Introduction of more complex dependencies for application of the APC to MAS prices.
- Timing of APC Applications to MAS prices (various parts of 3.14.2)
  - Retention of the current drafting relating to the timing of application of the APC to MAS prices.
  - Clarification that a MAS-triggered APP applies from the start of the next dispatch interval, or clarifying that the APP applies from some other point in time.

- Various miscellaneous issues, including non-controversial drafting refinements.
- Specific amendments to relevant sections as proposed by the NGF in their response to the first round Consultation Paper, and subsequently identified by AEMO, relating to the imposition of administered prices to neighbouring regions during the application of the MPC, MFP, APC or of the AFP in a region.

## **4.2 Historical Data Analysis**

The Commission conducted a review of the historical market data that related to the imposition of APPs, which was presented in Appendix B of the draft Determination<sup>15</sup>.

## **4.3 Principles for Determination**

In order to assess the issues and each of the respective options, the Commission reviewed the proponent's submission and the submissions to the Consultation paper and draft Determination, and drawing on these and its own research formulated a logical set of principles upon which it could make this Determination. These are laid out in the respective chapters below, which address each issue in turn. In coming to its Determination the Commission sought to satisfy the objective of having transparent, practical rules that intervene in market price setting only to the degree necessary to protect the long term interest of consumers.

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<http://www.aemc.gov.au/Media/docs/Draft%20Determination-fb9cdc60-d7a7-4452-ab08-c9db9cee5bd6-0.PDF>, page 30

## 5 Discretion to Extend an Administered Price Period

### 5.1 Rule Proponent's view

The rule proponent regards the discretion to extend an APP as unnecessary, and considers that *"it is inappropriate for AEMO and the AER to have discretion to impose an APP for a future period, based on an assessment of projected future price outcomes."*<sup>16</sup>

The rule proponent proposed that the relevant discretion of AEMO be removed, by deleting clause 3.14.2(c)(3). If this proposal is not accepted, the proponent proposed that the discretion be replaced with *"an objective test limited to and based on projected pricing outcomes in the pre-dispatch timeframe."*<sup>17</sup> The proponent also proposes to remove AER's role in consenting to AEMO's extension of an APP under either solution.

### 5.2 Stakeholder views

The views put forward in the respective consultation rounds are summarised in order here. Specific points are responded to in the appendices.

#### 5.2.1 First round of consultation

All three respondents stated in their submissions to the Consultation Paper a preference for the option of an objective test, rather than removal of the AEMO's power to extend. TRUenergy also stated a preference for the removal of the AER from the process, highlighting that the involvement of the regulator in operational interventions could create conflict of interest should that regulator later wish to conduct investigations into the market outcomes or into the behaviour of participants<sup>18</sup>. The AER considered that basing the decision to extend an APP on the pre-dispatch schedule would achieve a similar result to the current arrangements, but without the existing ambiguity and administrative difficulties<sup>19</sup>.

#### 5.2.2 Second round of consultation

The Commission in its draft Determination determined to delete the clause that gives rise to the extension of APP's ahead of time. In response to the draft determination, the AER<sup>20</sup> disagreed with this position, arguing that:

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<sup>16</sup> AEMO, *National Electricity Rule Change Proposal - EM 2010/002*.

<sup>17</sup> AEMO, *National Electricity Rule Change Proposal - EM 2010/002*.

<sup>18</sup> TRUenergy, *National Electricity Amendment (Application and Operation of Administered Price Periods) Rule 2011*.

<sup>19</sup> Australian Energy Regulator, *Submission to Application and operation of Administered Price Periods Rule Change Proposal (Ref: ERC0121)*

<sup>20</sup> Australian Energy Regulator, *Re: Application and operation of Administered Price Periods* 26 August 2011.

- removing the clause could potentially increase price volatility and exposure to extreme spot prices;
- the alternative option to extend the APP automatically based on forecast price data in the pre-dispatch schedule is not discretionary, and so the uncertainties for participants are lessened;
- removing the clause may increase uncertainty in the market, as administered pricing could cycle on and off each day, leading to significant volatility; and
- while generators may have the ability to influence pre-dispatch prices, this risk is outweighed by the benefits of avoiding possible off / on cycling of administered pricing. AER noted that manipulation of forecast prices through rebidding is subject to good faith provisions in clause 3.8.22A.

### 5.3 Other relevant considerations

The Commission stated in its draft Determination that it considers that AEMO's discretionary power to intervene should only be retained if the benefit gained by exercising it can be reasonably expected to at least offset the uncertainty its existence creates for participants.

With regard to the potential increase in exposure to extreme spot prices that might be caused by abolishing APP extensions made ahead of time:

- the Commission does not necessarily wish to prevent high prices that result from healthy market behaviour;
- the Commission considers following its scenario analysis that the extension of APPs ahead of time could lead to inefficient interventionary pricing outcomes; and that
- while the possibility of cycling of APPs on and off from one day to another would be highly unlikely, the pricing outcomes would be comprehensible and transparent to participants.

AER highlighted that an objective test based on pre-dispatch is not in fact discretionary as AEMO would have no decisions to make. The Commission accepts this point, but notes that the objective test would feature a swap of uncertainty caused by discretion for uncertainty caused by the use of forecast prices. With regard to the use of these forecast prices, the Commission is of the view that this could feature significant uncertainty, stemming from:

- natural day-ahead forecast error on key variables, for example demand and availability; and
- the ability of generators to influence the forecast with the option to re-bid closer to the time of dispatch.

On balance the Commission does not consider that the avoidance of cycling or repeated APPs outweighs the uncertainty created by the introduction of an objective test based on the pre-dispatch schedule.

#### **5.4 Conclusion**

The Commission has determined consistent with its draft Determination to delete clause 3.14.2(c)(3) and remove the application of APPs ahead of time.

## 6 Dependency of Administered Price Cap to Market Ancillary Services

This chapter considers those aspects of the rule change request that relate to clarifying what happens when an APP is triggered by one of the eight MAS.

### 6.1 Rule change proponent's view

The proponent argues that the clauses as currently drafted are ambiguous as to which of the eight ancillary service prices are capped when an APP is triggered by a single cumulative ancillary service price exceeding the CPT.

The proponent argues with reference to relevant Code Change documentation published by the National Electricity Code Administrator (NECA) (application) and the ACCC (authorisation) that the meaning of the clauses should be such that whenever an APP is triggered by a MAS, then all eight MAS prices are capped by the APC, but that energy prices should not be capped. The proponent also notes that AEMO presently interpret the clauses in this way in operating the market.<sup>21</sup>

### 6.2 Stakeholder views

#### 6.2.1 First round of consultation

In its first-round submission, the NGF argue that an APP triggered by Raise service prices should not cause prices for Lower services to be capped; and vice versa. Further, the NGF suggest that there would be expected to be a high correlation between high prices in one type of Raise service and another (or Lower service and another), and that these should be capped together; as the additional complexity involved in only capping one would be of little benefit.<sup>22</sup>

TRUenergy highlighted that not all plant capable of providing MAS can provide all eight MAS services, and this could create a risk because capping all eight services when only one is under stress could adversely affect providers of just one or a few of the other services. TRUenergy support the capping of the particular MAS that caused the APP to be triggered, but failing that, ask that the Rules should be amended to clearly state whatever option is decided upon.<sup>23</sup>

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<sup>21</sup> AEMO, *National Electricity Rule Change Proposal - EM 2010/002* page 4

<sup>22</sup> NGF, *Consultation Paper: Application and Operation of Administered Price Periods - ERC0121*.

<sup>23</sup> TRU Energy, *National Electricity Amendment (Application and Operation of Administered Price Periods) Rule 2011*.

### 6.2.2 Second round of consultation

The Commission stated in its draft Determination its preference to cap all eight MAS prices whenever a particular MAS price caused an APP to trigger.

The NGF disagreed<sup>24</sup> with this draft decision, arguing that periods of high price in both Lower and Raise services were possible during an APP, because the APP can span periods of high and low demand. This argument tends to counter the Commission's conclusion that there would be very little harm in capping all eight together. The NGF proposed the independent application of the APC to the four Raise or Lower services based on which type of service triggered the APP.

The NGF also disagreed with the decision not to implement a more detailed solution to the potential incentive that could be created to withdraw volumes from Raise services during a Raise-triggered APP. The NGF argued that the Commission's preferred approach, to simply allow AEMO to use its powers of direction and to rely on compensation arrangements as needed should the issue arise operationally, did not best promote the NEO.

### 6.3 Other relevant considerations

The Commission notes the arguments put forward by the NGF, and accepts that capping all eight MAS services when only one type of service is under stress could lead to unnecessary interventionary outcomes.

AEMC staff liaised with AEMO prior to the draft Determination with regard to the likely costs of implementing a solution in the market systems which independently applies the APC to each type of service. Though no detailed costing was carried out, broad estimates for the cost of implementation would likely be in excess of \$100,000. The Commission remains of the view that this option is not good value for money and hence not in the long-term interest of consumers when considering:

- the low likelihood of a MAS-triggered APP event occurring, let alone the likelihood of Lower services exceeding the APC during a Raise-triggered APP (or vice-versa);
- the provisions in place for AEMO to issue directions to participants in order to maintain system security; and
- the provisions for compensation to be afforded to generators affected by the imposition of APPs under the rules.

The Commission is of the view that the NEO is better served by not implementing the change because of the costs involved relative to the benefits the change would provide.

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<sup>24</sup> National Generators Forum, *NGF Response to AEMC Draft Determination on "Application and operation of Administered Price Periods" during high frequency response prices.*,

A similar conclusion is drawn with regard to the potential implementation of a more sophisticated capping arrangement for MAS prices during a MAS-triggered APP, such as that contemplated in the draft Determination. The Commission considered in detail what such a potential solution may look like, but remains of the view that the cost of implementing such a solution would be unlikely to be in the long-term interest of consumers, for the same reasons given above.

#### **6.4 Conclusion**

The Commission has determined consistent with its draft Determination to clarify that the wording of 3.14.2(d2) means that all MAS prices are capped during a MAS-triggered APP, rather than just one or a subset of different MAS prices.

## **7 Timing of Administered Price Cap to Market Ancillary Services**

This chapter considers those aspects of the rule change request that relate to clarifying the time that an APP is to commence following the exceedance of a cumulative ancillary service price above six times the CPT.

### **7.1 Rule change proponent's view**

The rule proponent argued that it does not appear reasonable to apply an APP only from the beginning of the next Trading Period when an ancillary service price exceeds the threshold part-way through a trading interval. The proponent requests that "*Where an ancillary service price exceeds the ancillary service price CPT threshold, the NER should make it clear that the APP commences immediately following the dispatch interval that exceeded the ancillary service price CPT threshold. This would provide certainty for Registered Participants and AEMO.*"<sup>25</sup>

### **7.2 Stakeholder views**

#### **7.2.1 First round of consultation**

TRU Energy and the NGF argue in favour of the proponent's proposed clarification.

#### **7.2.2 Second round of consultation**

In its draft Determination, the Commission considered that an APP triggered by an ancillary service price should commence in the dispatch interval immediately following the dispatch interval in which the CPT was exceeded. No comments were received on this matter in the second round of consultation.

### **7.3 Conclusion**

As no comments were received to the draft Determination on this point, the Commission has determined consistent with its draft Determination that clause 3.14.2(c)(1A) be clarified as proposed by the proponent to state that an APP triggered by an ancillary service price is to commence in the dispatch interval immediately following the dispatch interval in which the CPT was exceeded.

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<sup>25</sup> AEMO, *National Electricity Rule Change Proposal - EM 2010/002*.

## **8 Extension of Time for AEMO to include Compensation from Administered Price Periods, Market Price Caps, or Market Floor Prices**

The proponent proposed an extension to the time that AEMO may take to include compensation payable from an APP, MFP or MPC event in preliminary and final statements. The existing time period is 15 business days. The proponent contends that in some cases, 15 business days is not enough time to comply with its obligations, depending on the date at which AEMO is notified of the compensation amount payable and the position of that date relative to the ongoing settlement calendar.

The proponent has proposed to increase the time that may be taken to 25 business days. TRUenergy suggested in their response to the first round of consultation that the impact on Participants of this extension from 15 to 25 days would likely be minimal, provided that such extension furthers the efficient operation of the market<sup>26</sup>.

The Commission stated in its draft Determination that it was satisfied that the proponent's case for an increase in the allowed time as laid out in the rule change request is reasonable. The Commission has determined consistent with its draft Determination, that clause 3.15.10(c) be amended to allow AEMO up to 25 business days to fulfill its obligations to include compensation awarded by the AEMC under clause 3.14.6 in statements provided under clauses 3.15.14 and 3.15.15.

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<sup>26</sup> TRUenergy, *National Electricity Amendment (Application and Operation of Administered Price Periods) Rule 2011*.

## 9 Miscellaneous Amendments

### 9.1 Minor Drafting Changes

The proponent made several other proposals for change to the Rules, which are chiefly clarifications . These are laid out below:

- Include a reference to the term 'dispatch prices' in 3.14.1(a), and employ a transitional provision to give this effect,
- In clauses 3.14.1(a), 3.8.24(b), 3.9.2A(d), 3.13.7(e)(3) and (4), 3.14.1(a) and 3.15.7(c), omit "market" and italicise the term "ancillary service prices" wherever occurring,
- In clause 3.9.2B(e)(1) omit "market ancillary services prices" and substitute with "ancillary service prices" italicised,
- Delete clause 9.45.2, which explicitly stipulated the value of the APC in Tasmania and is no longer required

The Commission stated in its draft Determination that it considers that all of these proposals are merited in the interest of improved clarity in the Rules. As no submissions were received in the second round of consultation on these amendments, the Commission has determined consistent with its draft Determination that these amendments be made as proposed.

### 9.2 NGF Proposal - Clause 3.14.2(e)(4)

In its submission to the Consultation Paper, the NGF identified what they considered a logical error in the drafting of Clause 3.14.2(e)(4), and proposed that the clause be amended as part of this Rule Change.

The submission argued that the wording "*... that have an energy flow towards that regional reference node ...*" is incorrect and should instead refer to flows *away from* the regional reference node at which the AFP has been used to set the dispatch price.

As laid out in the draft Determination, the Commission considered that this proposal has merit and further, that a similar modification should be made to clause 3.9.6A(c).

As no submissions to this aspect of the draft Determination were received, the Commission has determined consistent with its draft Determination that clauses 3.14.2(e)(4) and 3.9.6A(c) be amended to refer to flows away from the region in which the APP is in force.

### 9.3 Further Consultation - loss factor references

In its submission to the second round of consultation (draft Determination), AEMO identified additional clarifications that it believes should be made to the two clauses

addressed in 9.2 above in relation to the application of loss factors. AEMO has also proposed that similar amendments should be made to the clauses that describe the inter-regional constraining of prices under the application of a Market Price Cap (MPC) or an Administered Price Cap (APC) (clauses 3.9.5(c) and 3.14.2(e)(2) respectively).

Because the proposal featured amendments to clauses that had not been the subject of consultation, the Commission published a further consultation paper under section 107A of the NEL<sup>27</sup> on 23 September 2011, seeking comments from stakeholders in relation to the proposed changes, and included a subsequent proposed amendment to the clause which constrains pricing during market suspension (clause 3.14.5(m)).

No submissions were received in response to the further consultation. Consequently, the Commission has determined that clauses 3.9.5(c), 3.9.6A(c), 3.14.2(e)(2), 3.14.2(e)(4) and 3.14.5(m) be amended as laid out in the further consultation paper and draft Rule to clarify that the loss factors applying to the direction of flow are to be used in the calculations.

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<http://www.aemc.gov.au/Media/docs/Further%20Consultation%20Paper-53b3b41b-be33-484c-b05f-831f8c9e2bf7-0.PDF>

## Abbreviations

ACCC	Australian Competition and Consumer Commission
AEMC, Commission	Australian Energy Market Commission
AEMO, proponent	Australian Energy Market Operator
AER	Australian Energy Regulator
AFP	Administered Floor Price
APC	Administered Price Cap
APP	Administered Price Period
CPT	Cumulative Price Threshold
MAS	Market Ancillary Service
MCE	Ministerial Council on Energy
MFP	Market Floor Price
MPC	Market Price Cap
MWh	Megawatt-hour
NECA	National Electricity Code Administrator
NEL	National Electricity Law
NEM	National Electricity Market
NEO	National Electricity Objective
NER	National Electricity Rules
NGF	National Generators Forum

## A Summary of issues raised in submissions

The submissions to the first round of consultation are reprinted below in section A.1, along with the original comments provided by the AEMC to those submissions as part of the draft Determination. The next section (A.2) covers submissions to the draft Determination and the AEMC's consideration of those submissions.

No submissions were received to the further short consultation paper regarding clarification of the use of loss factors in setting price caps and floors.

### A.1 First round of consultation

The submissions to the first round of consultation are reprinted here, along with the original comments provided by the AEMC to those submissions as part of the draft Determination. The next section (A2) covers submissions to the draft Determination and the AEMC's consideration of those submissions.

Stakeholder	Issue	AEMC Response
Australian Energy Regulator	Agree that 3.14.2(c)(3) [Discretion to extend an APP] is difficult to implement.	While this view is noted, following analysis and review of the historical information, the Commission considers that the removal of the clause will not lead to material risk of increased volatility, or material risk of increased exposure to extreme spot prices.  Commission is of the view that the pre-dispatch objective test is exposed to both implementation and legitimacy issues; and considers it inferior to either abolishment of the relevant clause or continuation of the opinion-based approach.
Australian Energy Regulator	Support amending rather than removing 3.14.2(c)(3), as removal could potentially increase price volatility and the risk that market participants are exposed to extreme spot prices for a protracted period.	
Australian Energy Regulator	Support extension of APPs based on the pre-dispatch schedule, arguing that the approach achieves similar result to the current arrangements, but without existing ambiguity and administrative difficulties.	

Stakeholder	Issue	AEMC Response
National Generators Forum	Support the option to retain AEMO / AER discretion to extend an APP when the CPT is not breached by use of the predispach schedule. Argue that it is important to retain an option to extend the APP, and that replacing AEMO discretion with an objective test would give participants greater certainty and better ability to manage risk. NGF go on to state that the use of an objective test could be 'gamed' by Generators seeking to manipulate the predispach outcomes, but then note that the triggering of an APP would in itself lead to a high likelihood that the test would not be needed, reducing the power of generators to game it.	Commission agrees that the test could be subject to gaming by Generators, and that the need to apply the test should be rare. However the Commission considers that the low likelihood of the test being needed is not sound justification for creating it.
TRU Energy	Support amending of 3.14(c)(3) in accordance with option 3(b) of the proposal, such that discretion to extend an APP be based purely on an objective test as proposed by the proponent. Also suggest removal of the AER from the process for practical reasons and potential conflict that could arise given the <i>ex-post</i> investigative powers of the AER.	As above in relation to the objective test.  Regarding the role of the AER, the Commission agrees that if AEMO's discretion were to remain that it would be preferable to remove the AER from the process.
National Generators Forum	Argue that the dispatch interval should be used as the basis for the rules relating to APPs; more broadly including for APPs relating to / triggered by energy as well as MAS prices.	The Commission considers that the possibility of moving the timing of energy-triggered APPs to the five-minute basis would more rightly be explored as part of any broader review on the timing of energy pricing.
TRU Energy	Agrees with the proponent and submits that the option whereby the APP is applied in the dispatch interval immediately following the dispatch interval in which the breach of the CPT occurs should be adopted.	The Commission agrees and this is reflected in the drafting of the Determination.
National Generators Forum	Argue that an APP triggered by Raise service prices should not cap Lower service prices and vice versa.	Commission agrees with these views in principle, but considers that the capping of all eight ancillary service prices during a MAS-triggered APP

Stakeholder	Issue	AEMC Response
	<p>Argue that there would be expected to be a high correlation between high prices in one type of raise service and another (or lower service and another), and that these should be capped together as the additional complexity involved in only capping one would be of little benefit.</p>	<p>will not create material distortions or risk to Participants or system security. The Commission considers that the cost of separating the capping of Raise and Lower in the software systems would not be offset by a sufficient increase in market efficiency or transparency.</p>
<p>TRU Energy</p>	<p>Argue that not all plant capable of providing MAS can provide all eight MAS services, and this could create a risk that capping all eight services when only one is under stress could adversely affect providers of just one or a few of the other services. Consequently support the capping of the particular MAS that caused the APP to be triggered. Failing that, Rules should be amended to clearly state whatever option (under Question 2) is decided upon.</p>	<p>Commission notes these views, but considers that the possibility of capping only the single service that caused the APP to trigger, could create unwanted incentives for providers to withdraw volume from that service, and move to other services instead.</p>
<p>Australian Energy Regulator</p>	<p>Do not consider that the current CPT/APP mechanism as a whole achieves its purpose in managing spot price risk. Highlights that the APP cannot prevent generators from manipulating the spot price to a level that comes close to, but does not exceed the CPT for a number of days. Argue that Generators can thus potentially structure their bids to maximise returns without triggering an APP.</p>	<p>The Commission agrees that the architecture of the CPT/APP mechanism and the existing settings of the APC and CPT would strongly encourage a price-manipulating Participant to prevent an APP from triggering in the first place. This point has helped to underpin the logic used to formulate this Determination.</p> <p>The Commission's investigation of the historic examples, including the 'near miss' of June 2007 did not extend to an assessment of whether the energy price was being manipulated in the way suggested in AER's response.</p> <p>It is noted that the historic examples do show the APC binding on several key days during the APP, removing the exposure of consumers to sustained spikes on those days. The Commission considers that, absent concerns about price manipulation and the intentional avoidance of APPs, the four APPs that have occurred in the NEM appear to have served their</p>

Stakeholder	Issue	AEMC Response
		purpose relatively well.
Australian Energy Regulator	Argue that there is a need to review the CPT and in particular its role as the primary risk management mechanism in the NEM. Suggest the next review of the Reliability Standards and Settings in 2012 would be the appropriate vehicle for this.	The Commission agrees that the Reliability Standards and Settings workstream is best placed to consider any change to the application and / or operation of the CPT.
National Generators Forum	Considers that the likely incidence of APPs due to MAS is so low that there will be little effect on the longer term market incentives. Hence, consider that the questions relating to long-term incentives should not be afforded any weight.	Whilst the Commission agrees that APPs triggered by MAS are unlikely to occur, it is still important to consider the directional impact of the Rule Change on incentives (both long and short term).
National Generators Forum	Argue that the main consideration in making determination should be the risk to system security, and that any increase in the need for AEMO to use its discretion should be avoided.	Commission agrees with this view but has also considered the impact on the economic efficiency of market outcomes, and the impact on transparency and certainty for Participants in coming to this draft Determination.
National Generators Forum	Highlight risk to system security that may arise if an APP triggered by a MAS produces market incentives to withdraw bids for the services that have been capped.	The Commission believes that this is a key point that has been highlighted by the NGF, and has considered its implications in depth in compiling this draft Determination.
National Generators Forum	Raise detailed issue regarding a logical error in clause 3.14.2(e)(4), arguing that the wording should be reversed to refer to flows 'away from' a region that is subject to administered price floor, rather than 'toward'.	The Commission considers that this is indeed a logical error and that the amendment should be made as suggested by the NGF. Consequently the draft Determination includes the explicit amendment of clause 3.14.2(e)(4) to refer to flows away from the region that is subject to an administered price floor.
TRU Energy	The complexity of the interactions between energy, the eight different MAS services, and the reaction and commercial decisions of the providers of MAS make it difficult to predict what may or may not happen once an	The Commission agrees with this point, but considers it important to seek to assess the incentives and disincentives created by the various pricing rules incoming to determinations.

Stakeholder	Issue	AEMC Response
	APP is triggered.	
TRU Energy	Note that when an APP is triggered by a MAS service, then there has by definition been a period of high prices preceding that time, and large revenues have been earned as a result. However, MAS providers may rely on short isolated periods of high price in order to cover their costs.	The Commission notes this point.
TRU Energy	Argue that the combination of infrequency of APP events, and the lack of complete information, makes the risk of exertion by a participant of influence over the imposition of an APP very low.	The Commission considers that the question of historical or potential future influence by Generators over the imposition of an APP is as yet neither proven or disproven, but that the risk exists in principle and should thus be considered as part of the rule making process where relevant.
TRU Energy	Suggest that the impact of an extension to the time proposed to make compensation payments following a market price cap, price floor or APP would be minimal, providing the extension supports the efficient operation of the market.	The Commission notes this view and weighs it heavily given TRU Energy's potential exposure to the impact of an increased time allowance. The Commission is satisfied that the proponent's case for an increase in the allowed time is reasonable.

## A.2 Second round of consultation

Submissions to the draft Determination are summarised here:

Stakeholder	Issue	AEMC response
Australian Energy Regulator	Removing clause 3.14.2(c)(3) could potentially increase price volatility and increase the risk that market participants are exposed to extreme spot prices.	Commission notes this view but considers this possibility is preferred to the uncertainty created by automatic extension of APPs ahead of time.

Stakeholder	Issue	AEMC response
	Support use of the pre-dispatch schedule in deciding to extend administered pricing, arguing that this would not be discretionary, reducing uncertainty.	As above
	Argue that deletion of clause 3.14.2(c)(3) may increase uncertainty as administered pricing periods could cycle off and on.	Commission accepts this is a possibility, but considers the possible 'cycling' effect to be transparent compared to other options. Also considers the cycling behaviour to be unlikely to emerge in practice.
	Consider that the unwanted potential incentive to influence pre-dispatch prices would be outweighed by the benefit of avoiding off / on cycling of administered pricing.	Commission notes this argument but differs in view on this point.
National Generators Forum	Request the AEMC note this consultation should not imply acceptance of the way the NEM dispatches and recovers the cost of MAS services provided by generators.	The scope of this Rule change does not extend to the broader arrangements for ancillary services, so no direct comment is provided in this paper.
	Argue that the APP should not apply to Raise and Lower frequency services at the same time. Highlight possibility that high prices in raise and lower services could occur during a single APP due to length of time the APP may be in place.	Commission accepts the possibility that a single APP could feature high prices in Raise and Lower at various times, but considers that the benefit of independently capping Raise and Lower would not be worth the cost of implementing the change in the market systems.
	Consider that administered pricing of the MAS raise services should feature capping at the maximum of the APC or the energy price during.	Commission notes this view but, as above, considers that this solution would not be worth the cost. Further, the solution would feature a moving price cap which would come at some cost to

Stakeholder	Issue	AEMC response
		transparency and predictability.
	Should the AEMC decide to pursue solution in draft Determination w.r.t. above point, NGF recommend a stated expectation that affected generators be compensated adequately.	The Commission notes that the rules already make provision for compensation to generators affected by the imposition of an APP.
Australian Energy Market Operator	Suggest various minor amendments in relation to the application of average loss factors in the APP clauses.	These suggestions were subject to further consultation, and have been adopted with adjustments by the Commission in formulating the Rule.