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AEMC
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By electronic submission: www.aemc.gov.au

Dear Sirs,

Draft Amended Compensation Guidelines EPR0023

The National Generators Forum (NGF) appreciates the opportunity to comment on the draft amended guidelines. One of our members, IPRA has a particular interest in this matter since their Synergen Power asset was involved in the initial application of the current guidelines.

In addition to these comments, the NGF also encourages the AEMC to commence its earlier foreshadowed review of the administered pricing arrangements as soon as possible. The Synergen compensation claim identified some substantive issues beyond the context of the Guidelines that require consideration. Improved clarity of the cost recovery arrangements, in particular, should be key element to that review.

Some issues relevant to such a review are set out below.

We will make comments in two broad categories –

- Comments on the currently proposed content of the guidelines, and
- Identification of apparent drafting errors in a relevant Rule clause, 3.14.6 that have the potential to adversely affect participants contrary to the apparent intent of the Rules, namely the provision of compensation. In relation to these matters we propose that the Commission consider two parallel actions. Firstly, ensure that these matters are considered in the planned review of clauses 3.14.6 and 3.15.10. Secondly, modify the guidelines to ensure that participants will not be adversely affected by any identified drafting errors in the period before these are rectified.

1. Comments on proposed guideline contents

1.1 Inconsistent principles applied to different categories of participants

In relation to scheduled generators, it is clear from the proposed guidelines that the intention is that the total of market revenue and compensation will not exceed the identifiable costs of the participant in maintaining supply during the application of the administered price cap and floor.

In contrast, the second paragraph of section 10.5 indicates that in the case of Scheduled Network Services the intention is to give a combination of revenue and compensation that will total the revenue that the participant would have received if the administered price cap and floor had not applied.

We submit that the application of such radically different principles to different classes of participant is not good regulatory practice.

We propose that either –

- Compensation for scheduled generators be increased so that revenue plus compensation will equal the expected revenue absent the administered price cap and floor, or
- Compensation for scheduled network services be redefined so that the sum of revenue and compensation covers only the identifiable direct and opportunity costs of the participant.

1.2 Guidelines incite some participants to disregard Rules

In section 10.4, there is provision for compensation to be based on a variable P_b which is defined as “estimate of bid price”. In support of this there are provisions for determining an “estimate of bid price” other than by reference to the actual bid in the market.

This can lead to compensation based on an intention that was not revealed to the market through the market bid. But if the market bid is not representing the true intention of the participant then the participant has failed to comply with the good faith provisions as set out in clause 3.8.22A.

If these guidelines allow compensation to be based on intentions that should have been revealed to the market in accordance with clause 3.8.22A, but were not, then this can be regarded as incitement to these participants to disregard Rule 3.8.22A.

We propose that compensation for scheduled loads be based only on market intentions as revealed in market bids.

1.3 Drafting comments on proposed guidelines

The appendix includes excerpts from the draft amended guidelines with drafting suggestions marked up.

These comments are additional to the major issues raised above, and do not include remedies for these issues discussed above.

2. Apparent errors in clause 3.14.6 of the Rules

2.1 Apparent errors in clause 3.14.6(c)(2)

Both clause 3.14.6(c)(2)(i) and 3.14.6(c)(2)(ii) refer to costs or opportunities foregone as “due to the application of the *administered price cap*, the *market price cap*, the *market floor price* or the *administered floor price* (as the case may be)” . However, we believe that there are actually no costs that are “due to” any of these events.

We contend that the facts are as follows –

- The costs incurred by participants in the relevant circumstances are due to the operation of their plant given the dispatch target produced by central dispatch,
- The dispatch process that produces these dispatch targets is unaffected by any of the *administered price cap*, the *market price cap*, the *market floor price* or the *administered floor price* . For any given set of market bids and offers (and other relevant inputs) the dispatch targets will be same regardless of these cap or floor prices.
- The consequence of the cap or floor price is not that participant costs are changed, but rather that market prices and hence participant revenue is changed and hence may not justify the physical operation of the plant in accordance with its dispatch targets.

We propose that the Rules be altered to be consistent with this reality, and that in the meantime costs incurred during the relevant period continue to be a basis for claim despite these costs not being due to the cap or floor imposed.

2.2 Apparent errors in clause 3.14.6(a)

Clause 3.14.6(a) makes the threshold issue for the claim of compensation that the spot price in a trading interval is less than “than the price specified in their *dispatch offer* for that *trading interval*.” This ignores that fact that price setting in the market is not based on the price specified in a dispatch offer, but rather on that price adjusted for losses in accordance with clause 3.8.6(b)(3).

The failure to recognise this fact may, at the margin, exclude participants who on the basis of logic should be allowed to make a claim for compensation.

2.3 Apparent errors in clause 3.14.6(a1)

Clause 3.14.6(a1) makes the threshold issue for the claim of compensation that the revenue receivable in a trading interval is “less than the minimum requirement specified by its *network dispatch offer* for that *trading interval*.” . This ignores the fact that the revenue expectation for a scheduled network service is not simply the offer price, but also includes an additional amount to cover the losses in transmission within the scheduled network service, as set out in clause 3.8.6A(g).

The failure to recognise this fact has the potential to exclude from the entitlement to claim compensation, participants that on the basis of logic appear to have a valid claim.

2.4 Apparent errors in clause 3.14.6(a2)

Clause 3.14.6(a2) makes the threshold issue for the claim of compensation that the spot price in a trading interval is greater than “the price specified in the *dispatch bid* for that *trading interval*.” As in the case of clause 3.14.6(a), this provision fails to consider the adjustment for losses in accordance with clause 3.8.6(b)(3).

The failure to recognise this fact may, at the margin, exclude participants who on the basis of logic should be allowed to make a claim for compensation.

2.5 Apparent errors in clause 3.14.6(a3)

Clause 3.14.6(a) makes the threshold issue for the claim of compensation that the ancillary service price in a trading interval is less than “the price specified in the relevant *market ancillary service offer*”. This ignores the fact that the pricing of ancillary services is not generally based on the price of the marginal ancillary service offer. The difference is due to the co-optimisation of energy and ancillary services dispatch and the common circumstance that the supply of an ancillary service will entail a change from the energy market dispatch target that would otherwise apply. For example a generator supplying a raise service will commonly need to be dispatched to a lower energy target that would otherwise apply, in order to allow “headroom” for the ancillary service provision.

This feature of the market dispatch process results in ancillary service prices that reflect not only the offer price for the service, but also the loss of energy market revenue by the participant that is a necessary part of the service provision.

The failure to recognise this fact has the potential to exclude from the entitlement to claim compensation, participants that on the basis of logic appear to have a valid claim.

2.6 Inaccurate statement of objectives

The statement of objectives of the compensation regime in clause 3.14.6, includes the following –

“...to maintain the incentive for:

(i) *Scheduled Generators, Scheduled Network Service Providers* and other *Market Participants* to invest in *plant* that provides services during peak periods; and...”

This conflicts with the nature of the compensation as specified in clause 3.14.6, which is specifically designed to avoid the compensation having any excess over the costs actually incurred in operation during the relevant period. Hence by definition during this period there is intended to be no contribution toward the cost of investment in plant.

We recognise that there is an expectation that the relevant times of price capping will be rare and brief, and hence that the periods for which there will be no contribution to investment incentives will have low materiality.

Nevertheless we suggest that the objective should be stated more precisely so as to avoid being in conflict with the detail of the compensation regime.

If you have any questions in relation to this submission, please call Ken Secomb on 03 9617 8321.

Yours sincerely



Malcolm Roberts
Executive Director

Appendix

Suggestions in relation to drafting

The following suggestions do not include the more significant issues raised in the body of this submission.

In 10.1 –

t = a Trading Interval for which a claim is being made.

In 10.2.3 –

ramping a unit beyond its normal operating mode or temporarily overloading a unit beyond its Maximum Continuous Rating (MCR), with potential consequences of:

Plant operators may chose to operate plant generally within the limits defined by the designer, because of degradation over time, or to increase the reliability of the plant or to extend its life. We propose that the normal operating mode should be reference point for any additional wear and tear.

In 10.3.2.1 –

- available alternative resources, which in turn, are determined by the demandsupply balance in the region, as well as that of interconnectors. Opportunity costs ultimately reflect, in one form or another, the prices of deploying these alternatives;

The reference here is to resources other than those controlled by the participant making the claim. The claimant cannot know the costs of these resources, only the prices at which they are offered to the market.

And also in 10.3.2.1 –

- uncertain events that may affect supply, for instance:
 - the breakdown of a gas processing plant or gas pipeline;
 - outage of pumping capacity (for a pump-storage hydro unit) for the limited energy resources; or
 - outages of other generators and transmission interconnections

The word “demand” does not appear to have any meaning in this context.

In 10.4 –

Note: It is assumed that the underlying dispatch does not change as a result of application of the administered floor price. It is, therefore, the reduced payment by the market for the increment of consumption reduction.