INFORMATION

Participant compensation following market suspension

Stakeholder submissions invited on draft rule

The Australian Energy Market Commission (AEMC) has made a draft rule that introduces a framework to compensate participants who incur loss during an electricity market suspension. Submissions are due by 4 October 2018.

Draft rule

The draft rule sets out a compensation framework that is designed to strike a fair and efficient balance between the interests of market participants and consumers. The compensation framework will apply if, during a market suspension, prices are set by the Market Suspension Pricing Schedule (MSPS) rather than by the normal dispatch and pricing process. Currently, there is no provision in the National Electricity Rules (NER) to compensate market participants for losses when the MSPS applies.

The aim of the framework is to ensure that, when prices in the MSPS are too low to cover generators' estimated short run costs, compensation is automatically payable so that generators do not incur loss. This is designed to remove the current incentive for generators to withdraw from the market when MSPS prices are low and await direction by the Australian Energy Market Operator (AEMO) (which results in the generator receiving compensation at the 90th percentile price). The draft rule aims to ensure that generators are not out of pocket when they provide services during a MSPS period, while also ensuring that consumers do not bear excessive costs associated with compensation payments.

The key features of the draft rule are:

- compensation will be payable to scheduled generators and ancillary service providers (who are also scheduled generators) if prices in the MSPS are not sufficient to cover their estimated costs
- estimated costs will be calculated using 'benchmark values': regionally-averaged estimated short run marginal costs for scheduled generators in each category (eg black coal, brown coal, open cycle gas turbine, combined cycle gas turbine, hydro, large-scale batteries) supplemented by a 10 per cent premium to account for divergences between estimated and actual costs
- where estimated costs exceed revenue earned by the generator under the MSPS, compensation is automatically paid to cover the gap - this reduces the risk that generators and ancillary service providers will incur loss due to low MSPS prices
- 'benchmark values' are to be calculated and published annually by AEMO using data already collected for planning purposes
- if automatically calculated compensation is insufficient or - where no compensation is automatically payable - revenue earned under the MSPS is insufficient to cover the generator's direct costs of participating in the market, a claim for additional compensation can be lodged with AEMO
- where a participant is eligible for automatic compensation under this framework, if AEMO is required to direct them to provide services during the MSPS period, the compensation automatically paid will be based on the MSPS compensation framework rather than the directions framework.

The Commission considers that the draft rule achieves AEMO's objective, minimises the potential for perverse incentives that could lead to inefficient outcomes, and achieves a fair balance between the interests of market participants and consumers. As a result, the draft rule will, or is likely to, contribute to achieving the National Electricity Objective as it

AUSTRALIAN ENERGY MARKET COMMISSION LEVEL 6, 201 ELIZABETH STREET SYDNEY NSW 2000
T: 02 8296 7800 E: AEMC@AEMC.GOV.AU W: WWW.AEMC.GOV.AU

promotes the reliability and security of electricity in the long term interests of consumers.

Submissions on the draft rule are due by 4 October 2018.

The draft rule creates an automatic compensation framework that operates during a MSPS period.

Background

AEMO may suspend the electricity and ancillary service markets where:

- a black system event has occurred
- it is directed to do so by a jurisdiction under a state of emergency
- it determines that the market is inoperable (eg due to IT failures or following a power system emergency).

Where the market is suspended, AEMO has two options to set electricity and ancillary service prices. If possible, AEMO will use the normal dispatch pricing mechanism. Where normal dispatch pricing is not possible, AEMO will set prices according to the MSPS (which is based on average prices in the preceding four weeks).

Market suspension events are rare, having occurred only twice since the NEM began: once as a result of an IT system failure in 2001 and the other following the black system event in South Australia (SA).

The rule change request

On 25 July 2017, AEMO submitted a rule change request proposing the development of a framework to compensate participants who incur loss due to the application of the MSPS. This rule change request followed the 13 day market suspension that occurred in SA in late 2016. During that event, prices were set in accordance with the MSPS.

AEMO noted in its rule change request that, during the SA event, the absence of a compensation framework meant some participants were incentivised to minimise financial losses due to low prices in the MSPS by withdrawing or reducing their availability for dispatch. As a result, AEMO was reliant on participant goodwill to manage system restoration and operation, or issuing directions so that participants who operated at a loss could recover their costs through the directions compensation framework.

AEMO considers that directions should be a last resort. They involve a resource intensive process and, if needed during a market suspension, create significant additional work at a time of already heightened control room stress. Directions are also inconsistent with the principle in the NER that AEMO decision-making should be minimised to allow market participants the greatest amount of commercial freedom to decide how they will operate in the market.

In proposing a new compensation framework for market suspension events, AEMO's aim is to remove the incentive for participants to await a direction in order to be sure that they can recover their costs.

AEMO proposed in its rule change request that the compensation framework applicable to Administered Price Periods (APP) be extended so it would also apply during periods in which the MSPS operates. Under the APP framework, each party that incurs loss makes a bespoke claim to itemise and substantiate their costs. The system is costly to administer and provides no predictability to market participants. Only one claim has been made under this framework since the inception of the NEM.

For information contact:

Senior Adviser, **Katy Brady** 02 8296 0634

Director, **Shari Boyd** 02 8296 7869

Media: Communication Director, Prudence Anderson 0404 821 935 or (02) 8296 7817

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