



Amending the administered price cap

Stakeholder submissions invited on new urgent rule change request

The Australian Energy Market Commission (AEMC) and other regulatory agencies have been reviewing market settings since the Australian Energy Market Operator (AEMO) was forced to suspend the wholesale electricity market in June, following an extended period of unprecedented volatility and extreme prices.

The AEMC has published a directions paper on an urgent rule change proposal from Alinta Energy to change the administered price cap (APC) to mitigate ongoing threats to the reliable operation of the NEM (National Electricity Market).

The proposed amendment to the APC seeks to ensure that prices during an administered price period (APP) are sufficient to cover the costs of most generators operating under today's market conditions to support normal market operation and settlement.

The AEMC is taking action to implement rules to manage the risk of major supply shortfalls in the future as the energy market transitions and to avoid the potential for costly and damaging blackouts for households and businesses.

Purpose of the Administered Price Cap

In June, a major blackout was only narrowly averted when the Australian Energy Market Operator, facing what it described as an “impossible situation”, issued nearly 500 emergency directions for offline generators to start generating power – but this approach is not sustainable over prolonged periods.

To protect customers from these situations in future, the AEMC has released a directions paper that considers a prudent change to the market settings to increase the Administered Price Cap (APC) in order to secure our electricity supply and keep the system stable as we transition to more renewable energy.

The APC can be thought of as a last-resort safety net which stabilises the electricity system by capping prices in the National Electricity Market during rare emergency situations, following a prolonged period of extreme prices.

The APC has only been used three times in the 24 years since the National Electricity Market commenced.

Alinta's rule change request

The rule change request from Alinta Energy proposes an increase in the level of the APC from \$300/MWh to \$600/MWh. Raising the APC to this level will enable more generators to supply additional electricity when it is needed most.

Importantly, the APC only caps prices during rare emergency situations. It has no impact on wholesale prices during the normal market conditions that operate most of the time.

Treatment as an urgent rule change request

Alinta Energy requested the AEMC consider the proposal as a request for an urgent rule under section 96(1) of the National Electricity Law. The proponent considers the rule change to be urgent as the current energy challenge on the east coast of Australia has threatened the effective operation and administration of the wholesale electricity market and the security and reliability of the interconnected system. Rule changes that are considered to be urgent may be processed under an expedited process under which there

is only one round of consultation and the AEMC is required to publish its final rule determination within six weeks of commencing the rule change process.

On the 8th of September the Commission extended the time frame for this rule to allow for the publication of this directions paper on 29 September. The extension of time is due to the complexity of issues raised by the rule change request and allows for more extensive stakeholder consultation through this directions paper.

Policy positions for consultation

This directions paper responds to stakeholder feedback on the consultation paper published in August 2022. It outlines proposed policy positions and seeks stakeholder feedback.

Stakeholders are encouraged to comment on these proposed positions as well as any other aspect of the rule change or this paper.

The two key policy positions proposed in this directions paper are:

- a temporary increase in the APC from \$300/MWh to \$600/MWh, to be implemented as soon as practicable and proposed to be in place until no later than 1 July 2025 when any change to the longer term setting of the APC would be made following the AEMC's consideration of the Reliability Panel's rule change request.
- no temporary change to the CPT.

It is anticipated that this temporary change to the APC will help the market and consumers to avoid the threats to system security and reliability that were observed in June during the recent application of the APC. This change is expected to reduce costly compensation payments that all electricity customers will have to pay because the APC is too low to cover their extra generation costs, and will support the transition to renewable energy by helping to keep the system stable.

Key dates

Submissions to the directions paper are due by **13 October 2022**. The Commission requests that where possible, evidence should be provided to support stakeholder submissions. Any confidential information can be treated as confidential and redacted from submissions published on the AEMC's website. The Commission also welcomes early submissions where possible.

The Commission intends to publish a final determination by **17 November 2022**.

Background on the APC, APP and CPT

The market operator AEMO, calculates the rolling seven-day cumulative spot market price in each region. When that cumulative price reaches a pre-defined level known as the Cumulative Price Threshold (CPT) in any region, the Administered price period starts and spot market prices in that region are capped by the Administrative Price Cap (APC). The APP continues and prices remain capped until the cumulative price falls back below the CPT. The CPT is designed to provide price signals to support the achievement of the Reliability Standard and manage potential risks to the overall integrity of the market. The CPT is indexed to movements in CPI. The Reliability Panel recommends the values that manage reliability including the APC and CPT and these are subject to consultation and set in a normal AEMC rule change process.

The APC is the maximum market price, in \$/MWh, paid to market participants in any dispatch interval, during an APP. The APC is currently \$300/MWh. By capping the maximum market price during an APP, the APC limits a market participant's spot exposure over that period. At the same time, the APC should provide sufficient spot revenue for the generators to cover their short-term costs and encourage participants to continue to supply energy through normal market mechanisms to allow the market to return to normal operation as soon as possible.

At the start of the NEM, the principal concern was the potential for systemic financial collapse as a result of a generator failure causing sustained high spot prices. Then, as

now, when a generator fails, it can face significant financial exposure against its hedging contracts, particularly if the failure results in high spot prices which then drive contract payments from the generator, for periods where it was unable to generate and earn spot revenue. Similarly, retailers with insufficient hedge contract cover may face purchasing some portion of their customer load from the market at prices significantly higher than they have contracted to sell to customers.

To determine the APC, the Commission attempts to balance:

- the risk of a systemic financial collapse of the electricity industry during an extreme market event is significantly reduced,
- compensation claims by market participants following an application of the APC are minimised, and
- market participants have appropriate incentives to supply electricity during administered price events and market signals for new investment are retained.

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