
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

<p>a. Is the proposed assessment framework appropriate for considering the proponent's rule change request?</p>	<p>Yes</p>
<p>b. Are there any other relevant considerations that should be included in the assessment framework?</p>	<p>The contractual and physical position of Alinta is relevant– Alinta could achieve a windfall gain to the detriment of end users if this proposed change were to be accepted. AEMC should also consider where the forward curves were for coal and gas at the end of 2021 (see the attached chart Cal 23 vs Daily Spot) and, in making any determinations, consider and appropriately account for how quickly forward curves can change vs the impact of an expedited rule change that appears to be made essentially to reduce administration.</p>

CHAPTER 6 – ISSUES FOR CONSULTATION: PROBLEM STATEMENT

<p>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?</p>	<p>The problem has not been appropriately identified. Coal fired generators were bidding above the cost of export parity for coal prior to the CPT being breached, although the gas linkage is clearer given the \$40 input cap price multiplied by installed heat rates.</p> <p>The recently increased cost of generation due to generators not locking in ample fuel supplies is the primary problem contributing to poor reliability of the market due to a lack of incentives to do so (such as in a capacity market), not the price cap.</p>
<p>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?</p>	<p>Yes but the proposed solution is not appropriate and may exacerbate the negative economic consequences. Simply doubling the wholesale price cap will likely place more financial stress on end users and retailers than already exists in the short term, and this cost will be passed on directly to consumers.</p>
<p>3. Does the rule change address the problem?</p>	<p>No – This rule change potentially rewards the cheapest fuel source and most expensive fuel source at the same level and does not reward suppliers that innovate to minimize energy costs.</p>

<p>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?</p>	<p>No, the rule change is not the best solution to the problem. Generators should be prevented from withholding capacity to maximize market prices. A meaningful price cap serves this purpose and incentivizes suppliers to search for cheaper and more reliable forms of generation. A better solution would be the combination of two key market design elements:</p> <ol style="list-style-type: none"> 1.) A capacity market that provides payment incentives for generators to offer energy commitments but simultaneously be fined for non-performance of agreed upon capacity obligations. 2.) A streamlined make whole payment system between AEMC and AEMO for excess fuel costs to be paid to individual generators in times of extreme scarcity.
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CHAPTER 6 – ISSUES FOR CONSULTATION: PROPOSED SOLUTION

<p>5. Is Alinta’s proposed amendment to the APC rule appropriate to address the problem?</p>	<p>No – Increasing the APC does not solve the problem of insufficient fuel supply procurement.</p>
<p>6. Given current commodity prices, what level of APC is appropriate to enable the normal market operation and settlement under an APP?</p>	<p>The current cap of \$300 appears to have been entirely appropriate given the outcomes: market intervention and a subsequent retracing of prices, together with a “post process” that forces transparency and accountability for bidding behavior. Any changes to the APC should be linked explicitly to fuel prices to provide exchange traded mechanisms for market participants to manage their risk.</p>
<p>7. What is the impact of such a change likely to be on generator and retailer risks borne in participating in the market?</p>	<p>Generators will immediately have a windfall gain as a low probability event will be priced into contracts as a high probability event. Retailers will be forced to hedge 100% of their load, leading very much to a less competitive marketplace and an oligopoly “gentailer”-led market with higher wholesale input costs & lower competition. End use customers effectively will have a “fuel” tax levied on them by generation owners.</p>
<p>8. How might the APC change to accommodate different commodity price assumptions?</p>	<p>The wrong question is being asked here: generator behavior led to the APC becoming an issue. In particular, coal generators bidding significantly above the export marginal cost of coal, and state-owned hydro also having very high-cost bid stacks. In our view, AEMC should consider an alternative stratified APC based on year ahead fuel costs alongside a capacity market obligation mechanism. Generators (both coal & gas) should not be rewarded for not hedging their fuel supply and should be fined for unreliability.</p>

<p>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?</p>	<p>See above at 8 – a stratified approach based on year ahead fuel costs, but generators should not be rewarded for not hedging their fuel costs. Raising the APC effectively does this. As an example, the cost of coal tripled from the end of last year to June this year. Generators exposed to the export price of coal had a choice to make last year and by not hedging their fuel source they exposed themselves to the global macro impact of war in Ukraine. This should not be a cost that is borne by retailers, customers and end users of energy.</p>
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CHAPTER 6 – ISSUES FOR CONSULTATION: TEMPORARY LEVEL OF THE CPT

<p>10. Is there any consequential need for a change to the CPT resulting from a temporary change to the level of APC?</p>	<p>No. This effectively rewards generators for not hedging their fuel costs.</p>
<p>11. Should the calculation of the CPT be different during the APP?</p>	<p>No.</p>
<p>12. Is there a more appropriate method of triggering the APC?</p>	<p>Not unless a long lead time is given, because the market is currently set up right now around the current process.</p>
<p>13. Should a temporary change to the level of the APC consider the interaction between the gas APC and electricity APC?</p>	<p>Yes.</p>

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

<p>14. What is an appropriate temporary timeframe for application? Considering the factors that require the rule change to be made including commodity price changes?</p>	<p>Assuming changes are to occur, then an appropriate timeline is to make any changes part of the 2025 market redesign plan such that a capacity mechanism can be coopted to any changes to the CPT or APC.</p>
<p>15. What consideration should be made of changes and the timing of changes to be introduced by the Reliability Panel?</p>	<p>The timing is key and as mentioned is driven by a company with a large physical long position via assets and an unknown financial position. Any shocks to the market will penalise retailers who are already covering the costs via the AEMC</p>

	compensation claims mechanism, then penalise them again with higher wholesale contract prices.
16. How should a temporary change in the level of APC accommodate changes to commodity prices during its application?	As described at 8 above, it should be stratified & benchmarked to each fuel specific cost.
17. What are the consequences for the retail and contract markets from one-off or sequential changes to APC?	Any short term or sequential changes to the APC will increase volatility in the wholesale contract markets. This will likely lead to increased costs through higher contract volatility.
18. Should there be a mechanism to ensure that the APC is dynamic and indexed with an appropriate commodity price?	This approach could work, but it would likely need to be indexed against specific fuel types otherwise dirtier fossil fuels may gain an unfair advantage in the process (why should brown coal win from this?).

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?	Generators are compensated for any proven adverse affects right now via the AEMC. If the APC is lifted to - say \$600 - that may reduce the number of compensation claims but has no bearing on whether a generator will actually run during APP periods, which means market suspension is still a real risk. History shows that when price caps are instituted, markets simply adjust such that the new cap is the "new normal" - this will do nothing for consumers.
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Cost of Energy

Contract market and financial requirements

<p>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?</p>	<p>All ASX forward power contracts will rally, caps & swaps will also rally by a broadly equivalent amount, and option products will see implied volatility levels increase. It is impossible to make an estimate how far these products will move, however it will likely only be in one direction – up.</p> <p>OTC products often contain force majeure clauses and similar language that may be triggered by this event, requiring legal action between counterparties.</p> <p>Any increase of the CPT will also have a similar effect. For example, if a rolling 7 days prices at \$600 instead of \$300 this results in a \$25 mark up to a quarterly contract. For the sake of this example, suppose that the market implies there is a 25% chance of this event happening the next 12 months so that equates to a \$6.25 lift on a calendar year product. Any change to the CPT will be similar.</p>
<p>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?</p>	<p>Retailer credit support requirements would very likely increase because of a temporary change in the APC or the CPT.</p>
<p>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?</p>	<p>The requirements for NEM bank guarantees and security deposits to support trading would very likely increase because of a temporary change in the APC or the CPT.</p>
<p>26. What costs are imposed by the imposition of a temporary change, on a market setting that is normally unchanging?</p>	<p>Margin increases, exit of small retailers, increased legal costs via force majeure, reduction of liquidity providers, significant increase to end use customers.</p>

Chart referenced Chapter 4

