



11 August 2016

Reliability Panel
Australian Energy Market Commission
P.O. Box 2449
Level 6, 201 Elizabeth Street
Sydney NSW 1235

By online submission on the AEMC portal

Thursday, 11 August 2016

Dear Reliability Panel Secretariat,

RE: Reliability Standard and Settings Guidelines – REL0059

ENGIE appreciates the opportunity to comment on the Reliability Standard and Settings issues paper prepared by the Reliability Panel.

ENGIE is a global energy operator in the businesses of electricity, natural gas and energy services. ENGIE is the number one independent power producer in the world with 115.3 GW of installed power-production capacity, 19 GW of which is renewable. ENGIE employs 1,800 people in Australia and supplies 12 per cent of Australia's National Electricity Market, and has an installed generating capacity of more than 3,550 MW. ENGIE also owns Simply Energy which provides electricity and gas to more than 550,000 retail customer accounts across Victoria, South Australia, New South Wales and Queensland.

This submission builds on our earlier submission regarding the Reliability Standard and Reliability Settings Review 2014 (REL0051/10/4/14; ENGIE was previously known as GDF Suez).

ENGIE supports the development of clear guidelines that state the purpose of the settings and outline the modelling methodology for undertaking the next review.

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Question 1 - Analytical framework

ENGIE acknowledges that trade-off between the various parameters is needed and suggests some changes to the stated objectives on p6 as follows:

- *“Maintaining stable and consistent regulatory frameworks, while allowing sufficient flexibility to account for changes in the market.*
- *Sending effective price signals ~~to drive~~ which support and don't impede efficient investment, while maintaining adequate protection for market participants from sustained high prices.*
- *Delivering Creating and maintaining an environment to support an acceptable level of reliability, at a price that matches the value that consumers place on reliability”*

ENGIE suggests that the first above dot point can be addressed by allowing a sufficient upward tolerance of the reliability parameters so that they do not need to be adjusted on a regular basis as they are under the current arrangements.

Notably, as the market is challenged by subsidised intermittent generation the incentives for parties to contract needs to be maintained. This is an issue that may not have been fully considered under the earlier analytical framework.

Question 2 – Matters to be considered

It is important to consider the function of the market price cap (MPC) and cumulative price threshold (CPT) and other matters prior to determining the methodology to quantify or set them.

For example, the MPC is a very important parameter and ENGIE does not agree with the view that it has reached its limits to incentivise a market response. The MPC does not only create generator and retailer response but also demand side. Both decisions to actively participate in the market and decisions to contract directly with generation.

By setting the MPC too low, supply or demand side response will be discouraged since some of the inherent risk in the market would be mitigated “for free” by the regulated price cap. This will in turn lead to reduced incentive to forward contract and hence impede liquidity in the contract market and eliminate some of the essential medium/longer term market signals. Essentially no investor (demand or supply side response) is prepared to invest for the one in ten-year event; they need some stable revenue stream (i.e. from selling caps).

It should be remembered that the MPC acts as an in-built cap on the market. Therefore, the counter-factual should be what behaviours would occur if this arbitrary cap was not in place. In ENGIE's view it is likely a more to facilitate and active demand response sector and encourage unsophisticated commercial players to contract and not ‘ride spot’ on the back of oversupplied intermittent generation.

In this context, risks of setting the MPC too low risk market failure and are considered far more detrimental to the market stability and efficacy than if the MPC is set too high.



A pragmatic approach is to set the MPC higher than determined by the modelling, (even after having factored in uncertainties and risks as outlined in our response to Question 3), to ensure it is “out of the way” and the market (supply and demand) can respond underneath it.

If this approach is adopted, it becomes less necessary to adjust the MPC by the CPI as its impact becomes a distant second order issue.

In this manner the major risk mitigation setting becomes, as it should be, the CPT. The MPC shouldn't reduce, at all, contracting incentives to avoid risk for individuals at a point in time, but it is appropriate that the CPT act as brake of aggregate risk. Therefore, the CPT should be set with reference to the amount of risk the market can manage in aggregate not simply as a function of the MPC. The two settings should be decoupled. This is an issue that has been raised over numerous reviews across many years but a number of market participants for which no detailed analysis has occurred.

In summary, by changing the approach to the MPC and CTP, the risks and impacts associated with changing the standard and/or settings are minimised or eliminated.

Question 3 – Modelling

The extreme peaker vs the cap defender approach

As a matter of principle, the modelling should not incorporate subjective assumptions regarding offer/bid behaviour or dispatch. To be sustainable, the cap contracts need to be valued at the expected value of a cap using the modelling output (without cap contracts in place). Cap contracts may serve to smooth the costs/revenues to counterparties but should not be used to change behaviours in the modelling.

Whether a generator would run below the MPC and when the price is above its marginal costs would depend on a range of considerations regarding its fixed and variable costs, including the cost of stay in business capital and expected asset life (perhaps quite short) as well as others.

Demand side response may value its response in a similar way and should be treated in a consistent manner to maintain technological neutrality and symmetry between supply and demand side.

ENGIE believes that the use of the cap defender approach is distortionary, misprices generation output or demand side response and therefore must not be used as a technique for the MPC determination. ENGIE believes the use of this approach undermined the value of previous work and strongly urges the AEMC to move away from this approach in the future.

Modelling inputs, sensitivities and scenarios

ENGIE agrees with the proposed range of inputs and assumptions, and scenarios and sensitivities but suggests they are augmented to include the following:

- Plant life and the level of WACC from an investors perspective
 - There is a high and increasing level of uncertainty of future environmental policy outcomes
 - Technology developments and risks



- Market risks
- Changing load shape
- Gas supply arrangements are complex and costly. To secure firm gas transport is also expensive.
 - This will increase costs to generators and customers and needs to be incorporated into the modelling assumptions.
- Transmission risks and costs
 - Transmission arrangements in the NEM are non-firm and present significant costs and risk to participants.
 - As the supply side is transformed over time, generating and consumption patterns will change and some existing constraints will grow whilst new constraints will materialise. These risks also need to be factored into the modelling (possibly adopting a higher WACC).

All of these elements serve to increase risks for investors and need to be addressed in the modelling. In ENGIE's view there is a case to argue that investment in the National Energy Market has been seriously compromised by policy interventions and therefore payback periods have been greatly shortened across all technology types.

ENGIE trusts that the comments provided in this response are of assistance to the Reliability Panel in its deliberations. Should you wish to discuss any aspects of this submission, please do not hesitate to contact me on, telephone, 03 5135 5363.

Yours sincerely,

David Hoch
Regulatory Strategy and Planning Manager