SUBMISSION

AEMC RELIABILITY PANEL RULE CHANGE – MPC, CPT, APC CONSULTATION PAPER – ERC0353

22 JUNE 2023

INTRODUCTION

The Energy Users' Association of Australia (EUAA) is the peak body representing Australian commercial and industrial energy users. Our membership covers a broad cross section of the Australian economy including significant retail, manufacturing, building materials and food processing industries. Combined our members employ over 1 million Australians, pay billions in energy bills every year and in many cases are exposed to the fluctuations and challenges of international trade.

The EUAA does not support the rule change as presented in the Consultation Paper ('Paper') because we do not consider the analysis presented by the Panel and the Commission is robust enough to justify that the changes are consistent with the NEO and the long-term interests of consumers.

Specifically:

- The NEM is no longer an energy only market but a hybrid energy/capacity market fast moving towards the capacity end of the spectrum. The introduction of a variety of capacity support mechanisms and jurisdictional policies clearly shows Energy Ministers have little faith in the ability of the energy only NEM to deliver the level of reliability they desired (political reliability). This suggests to our members that the additional benefits of the proposed large increase in MPC and CPT are not worth the cost to consumers. We look forward to the Commission in its Draft Determination providing the research that gives consumers confidence that they will not pay twice for the same level of reliability – once through jurisdictional schemes (such as the proposed Federal Capacity Incentive Scheme and the NSW storage LTESA scheme) and again through higher wholesale prices from a higher market price cap.

- The APC analysis completely ignores the impact of the Gas Mandatory Code on the appropriate level of the APC as it relies on now outdated analysis completed in 2022. There is no analysis of the actual compensation paid from the June 2022 APC event in assessing whether there is still 'undue reliance on compensation arrangements under high fuel price events. There is no analysis as to why a higher APC for all generation and storage is a lower cost alternative to either a $300/MWh cap and access to compensation or a more targeted support. This more targeted support would be in addition to the extensive support already provided under e.g. NSW Roadmap LTESAs, AEMO offtake agreements and the forthcoming Capacity Investment Scheme.

To be clear, our position on the rule change may change depending on the level of additional analysis provided in the Draft Determination and we are happy to engage with the Commission as it develops that additional analysis

CONSUMER INPUT

It is worth highlighting that the two consumer representatives on the Reliability Panel do not support the rule change. As the Information Sheet on the Panel's September 2022 report said[1]:

> "The majority of the Panel considers the final recommendation was justified given the value of the benefit the modelling indicated would be realised by consumers from enhanced future reliability outcomes. Two Panel members representing consumers, however, do not consider an increase to the MPC or CPT was required at this time for the reasons outlined in the final report."

We are surprised that while the Paper argues extensively for the changes to be in the long-term interests of consumers, it makes no mention of that lack of support. It is as if their views have been deleted from the record. It gives the impression that consumer views are no longer relevant and makes us wonder why we should even consider making a submission to the consultation paper. Despite these concerns, we feel it is still important to put a stake in the ground on behalf of EUAA members and to support the consumer representatives on the Reliability Panel.

RESPONSES TO THE PAPER

<u>The Panel is recommending reliability settings for an energy only market when in reality the NEM has moved from that and is fast moving further away from being one.</u>

The Information Sheet on the Panels September 2022 report said[2]:

> "The 2022 RSS review and final recommendation are provided in the context of the existing energy-only market design. The design and scope of a capacity mechanism and the interim reliability measure were out of scope for the 2022 review. The Panel has made some commentary on those issues, to the extent they intersect with the Panel's final recommendations on the reliability standard and settings."

The Paper discusses how the NEM reliability policy environment is changing with the implementation of jurisdictional schemes. These are both State based e.g. NSW Roadmap and Queensland Energy and Jobs Plan, and Commonwealth e.g. Capacity Investment Scheme (CIS). It notes that they provide investment support for new generation to meet reliability objectives. The Commonwealth Minister said the CIS[3]:

> "…will provide the national framework needed to drive new renewable dispatchable capacity and ensure reliability in Australia's rapidly changing energy market over the next decade and beyond.

[1] https://www.aemc.gov.au/sites/default/files/2022-08/Information%20sheet%20-%202022%20Reliability%20standard%20and%20settings%20review%20final%20report.pdf
[2] https://www.aemc.gov.au/sites/default/files/2022-08/Information%20sheet%20-%202022%20Reliability%20standard%20and%20settings%20review%20final%20report.pdf
[3] https://minister.dcceew.gov.au/bowen/media-releases/capacity-investment-scheme-power-australian-energy-market-transformation

This new revenue underwriting mechanism will unlock around $10 billion of investment in clean dispatchable power to support reliability and security as the energy market undergoes its biggest transformation since the industrial revolution."

What is puzzling is the Paper's comment (p.3):

"Given these schemes are additional measures to support reliability (in addition to emissions reduction), the Commission will consider how these schemes and the market price settings interact and the implications for the proposed changes to the settings."

We would have expected this discussion to be in this Paper. But none is provided. We would have expected analysis showing:

- What level of new generation capacity has been brought (or is expected to be brought) to market through these jurisdictional schemes
- What level of generation has been brought to market due to the MPC in the last 5 years and what is the expected new generation resulting from the proposed increase in the MPC i.e. generation that does not rely on any funding/revenue certainty through a jurisdictional scheme
    - Particularly given that the MPC is calculated on the basis of the open cycle gas turbines being lowest cost marginal new entrant in NSW – are OCGT's really going to be required under the NSW Roadmap and the CIS?
- Even if new OCGTs will be required in NSW, why is an increase in the MPC the most efficient method in the long-term interests of consumers to achieve that? Is an increase in the MPC the best method in the long-term interests of consumers to incentivise investment in storage when there is the Roadmap and CIS?
- How the Commission can, given its focus is the long-term interests of consumers, give consumers confidence that they are not paying twice for reliability –
    - once though higher wholesale prices from a higher MPC, and
    - once through the pass-through costs of jurisdictional schemes (e.g. NSW Roadmap LTESAs) or as a taxpayer through State Government GOC funding under the QEJP of the Victorian SECV 2.0

<u>The conclusion that the events of June 2022 continue to justify a $500/MWh APC is not supported</u>

The justification for the increase to $500/MWh in the Panel's report and $600/MWh from the Alinta rule change request in 2022 was based on two interrelated arguments:

- It would reduce 'undue reliance on compensation arrangements under high fuel price conditions'
- Generation would be more available at times of high fuel prices and so reduce the potential for USE

Both the Panel's decision and the Commission's decision on the Alinta rule change were made before the AEMC had processed generators compensation claims arising from the June 2022 events and before the Federal Government's decision on the gas price cap and mandatory code. It is surprising that the Paper makes only cursory reference to the former and no reference to the latter in its justification for the rule change.

Compensation costs to be paid by consumers

The Paper notes (p.11):

> "The Panel was mindful of the cost impacts of its recommended increase in the APC. The key cost identified by the Panel was the additional burden on retailers and consumers during an administered price period associated with compensation cost management and pass-through"

The Paper makes a qualitative argument for this based on the experience in June 2022. It is not clear if the argument is about administration costs or around the costs of the compensation to consumers. We believe the focus should be the latter.

On the former, the Paper refers to the Panel and Commission decisions being driven by concerns that keeping the APC at $300/MWh (p.10):

> "…would lead to undue reliance on compensation mechanisms which would increase uncertainty for consumers and retailers associated with the pass-through of these compensation costs."

Yet our reading of the actual compensation paid is that it is significantly less than many had predicted at the time[4]. Many of the original claims for direct cost and opportunity cost compensation have been withdrawn. In some cases, the AEMC is still awaiting further information from the claimant nearly 12 months after the events occurred. Only six decisions – all for direct costs – have been made.

Cost Category	Status at June 2023
Direct costs	
Withdrawn	10
Awaiting information	1
Not sufficient information	1
Formally commenced	1
Final decision published	6
Opportunity costs	
Withdrawn	10
Awaiting information	3
Formally commenced	2

Only six decisions – all for direct costs – have been made with no award of opportunity costs which was seen as a potentially large cost. The total costs for the six final decisions published so far is under $18m. Given the claims are confidential, we can only conclude that, in all cases except Basslink (where there are special circumstances in place), gas generators were not greatly impacted by paying high spot gas prices. It is difficult to see how this could be regarded as 'undue reliance on compensation'.

Claimant	Compensation received
Shell Energy Retail	$498,871
Smithfield	$592,256
Origin	$1,232,024
Braemer	$300,036
Basslink	$15,257,724

[4] https://www.aemc.gov.au/our-work/apc-claims/june-2022

Aurora	$206, 575
Total	$17,880,911

The Paper should have provided this data to help consumers decide on the merits of the rule change. We can understand the view that there was uncertainty for consumers back in August 2022 (when the Panel's report was being drafted) and November 2022 (when the Alinta rule change decision was being drafted). It was the first time this compensation mechanism had been used. However, we would suggest that any uncertainty in consumers' minds has now disappeared. We have a pretty good idea of what will happen next time – consumers are not worried about a significant cost pass though. But they are worried about the overall costs in wholesale electricity prices from a $500 or 600/MWh APC.

Will gas prices impact on generator willingness to bid?

The Paper relies on the analysis the Commission undertook for the Alinta rule change looking at the level of compensation required at high fuel costs. It notes (p. 10):

> "The Panel noted that the development of the LNG export industry had led to a stronger link to international prices but considered the probability of high fuel cost conditions similar to those experiences in June 2022 remains low."

While the chances remain low, the argument is that there is a risk of generators not being willing to bid at high gas prices where they have to rely on APC compensation to keep them whole. This may have been a reasonable conclusion in August/November 2022. The Commission has not made the case that it is still the situation. We would argue that the chances of high gas prices are considerably less than the 'low' probability in 2022 and generators are now very familiar with, and should have confidence in the process, applying for APC compensation – just as they are with directions compensation.

It is surprising is that the Paper makes no reference to the Government's gas price cap and Mandatory Gas Code which are explicitly designed to delink domestic prices from international prices and ensure sufficient supply is available to the domestic market. Last week the Government announced that design of the Code had been completed[5]:

> "The Gas Code will ensure Australian gas is available for Australian users at reasonable prices…
>
> Producers have already offered indicative domestic supply commitments under the new framework of at least 260 PJ to 2027. These indicative commitments will reduce the risk of shortfalls as assessed by the ACCC and AEMO.
>
> The final design of the Gas Code places a greater emphasis on:
>
> - Securing additional domestic supply commitments in the short term to anchor prices at $12/GJ and shield east coast gas consumers from volatile international gas prices.

[5] https://minister.dcceew.gov.au/bowen/media-releases/joint-media-release-new-gas-code-secures-supply-reasonable-prices-australian-users

- Facilitating certainty for investment in new supply to avoid projected shortfalls and sustain reasonable domestic gas prices over the medium term

  It will ensure domestic prices are reasonable by establishing a price anchor, a mechanism to drag prices down - through the combination of:

  1. A price cap, which is to be set at $12/GJ (with a review commencing by 1 July 2025)"

We would have expected the Paper to provide an analysis of why the $500/MWh APC is still required when the Mandatory Code is in place. That analysis would cover of the impact of the Code on generator gas contracting strategy:

- Given gas producer commitments to provide enough gas via contract to meet ACCC/AEMO forecasts that include GPG, how much GPG gas is likely to be sourced from contracts formally covered by the Code (from producers), how much from contracts effectively covered by the Code (from retailers) and how much sourced from the spot market that is not covered by the Code? And how this differs from history – or at least 2022?
- While the Code does not apply to the spot market, a likely impact of the Code on spot market prices will be to apply downward pressure (we have seen the impact of the $12/GJ price cap since December 2022)

We would suggest that the analysis used to justify both the Panel's decision on a $500/MWh APC and to the Commission's decision to approve a $600/MWh interim APC on the Alinta rule change is no longer relevant given the Mandatory Code. So, we do not agree with the Commissions view (p. 10):

> "The Commission is not intending to consult on retaining $300/MWh given the RSS Review and APC rule change both considered the existing APC level to be inappropriate. The Commission, therefore, intends to focus consultation on the relative merits of a $500/MWh or $600/MWh APC to apply over the review period."

This analysis would need to assume that the Government's objectives in introducing the Code are achieved. The gas price cap was reached in June 2022 because of a lack of gas volume. Those volumes are now being guaranteed by producers as well as AEMO having power to direct gas supply. So, the likelihood of generation at prices approaching the gas price cap, which requires a $500 or $600/MWh APC that was 'low' before the Code, is now very remote, if not almost eliminated, with the Code

If the Panel/Commission think there is an argument for a higher APC to support storage during an administered pricing period then they should make the case. Generally, we would expect that the storage purchases of power would occur during the day when prices were at a level that allows them to at least cover operating costs and cycling losses. If that is not the case, then they have access to the APC compensation mechanism.

Alternatively, why is a $500/MWh cap preferable to more targeted support for storage in addition to the extensive support that is available or about to be available e.g. NSW Roadmap LTESAs, AEMO offtake agreements and the forthcoming Capacity Investment Scheme.

In summary, there is no evidence provided that would support the view that the high fuel price conditions in June 2022 will return under the Gas Code which means there will be considerably less reliance on compensation. In any case the level of compensation paid out to generators following the June 2022 events is quite small. Our argument against the Alinta rule change was not that we disagreed with a change in the level, it was that the Commission had not mounted a case for a change[6]. The same argument applies here. We look forward to a different outcome this time.

Do not hesitate to be in contact should you have any questions.

Andrew Richards
Chief Executive Officer

[6] The Commission misrepresented the EUAA's view in the Alinta rule change https://www.aemc.gov.au/sites/default/files/2022-10/EUAA%20-%20LATE%20Stakeholder%20Submission%20-%20ERC0347%20-%2020221014.pdf