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MARKET POWER MITIGATION AMENDING RULES EXPOSURE DRAFT #2

Alinta Energy appreciates the opportunity to provide feedback on the second exposure draft of draft market power mitigation amending rules and recognises the changes made in response to our submission on the first exposure draft.

Alinta Energy provides the following comments and recommendations for EPWA's consideration.

If you would like to discuss this further, please contact me at oscar.carlberg@alintaenergy.com.au or on 0409 501 570.

Yours sincerely

Oscar Carlberg
Wholesale Regulation Manager

Alinta Energy's priority rating	Topic	Rule reference	Alinta Energy recommendation
Highest	General trading obligations and the STEM	2.16A.1 2.16A.2.	Alinta Energy considers that generators should be permitted to incorporate the following factors in their STEM offers. - <u>The opportunity cost of selling their capacity in the RTM instead.</u> For example, a facility that would be obliged under 2.16A.1 to offer its capacity at $40 in the RTM should not be required to offer this capacity at $40 in the STEM if $100 prices in the RTM are predicted the next day, all else being equal. If this participant is not permitted to incorporate the $60 opportunity cost of selling in the STEM rather than the RTM, it would be required to transfer wealth to other participants who can arbitrage its position in the STEM. Ultimately this would present a barrier to entry because it disadvantages participants with generation and storage capacity who are consistently required to make out of the money STEM offers. - <u>Additional allowances for uncertainty in renewable generation.</u> For example, in a hypothetical case where 500MW of wind capacity is expected in a participant's portfolio, we suggest that the participant should not be required to make 500MW of wind capacity available in their portfolio supply curve, noting the large risk that it won't be available in the RTM. Instead, the generator should be able to make much more conservative estimates about how much of their renewable capacity would be operating in the RTM, including for worst-case scenarios. - <u>Appropriate risk margins</u>. Risk margins can be described as the returns that speculators expect to receive as compensation for taking another party's natural exposure to fluctuations in prices through buying or selling a commodity futurescontract.[3] In the STEM, a risk premium is required as the generators are selling their capacity day-ahead, passing the price risk from the customer to the generator. Prohibiting risk premiums prevents them from being compensated for this price risk. We note that this price risk will tend to be one sided, as the requirement to offer into the STEM and the strict obligations about how to construct offers can suppress STEM prices below forecast prices in the spot market We are uncertain whether the proposed general trading obligations would permit this. We recommend that 2.16A.1 not apply to the STEM, or otherwise, that EPWA clarify whether these factors would be permitted or otherwise amend the obligations to ensure that they are for the above reasons.
Lower	General trading obligations	2.16A.2	Alinta Energy continues to question whether 2.16A.2 is necessary in the WEM for the reasons outlined in its previous submission.

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Highest	General trading obligations	2.16A.2	If 2.16A.2 is retained, Alinta Energy strongly recommends that it should not omit the words, "for the purpose of" which are included in the CCA sections it replicates. Doing so would increase ex-ante uncertainty and the potential for undue penalties because participants can be perceived to be distorting or manipulative prices, even where this was not the purpose of their behaviour. Under the CCA, there are two elements that must be present for the prohibition to apply: • the behaviour of a generator in the spot market; and • the characterisation and/or purpose of that behaviour. The second element looks to whether the behaviour has a particular character or purpose: a) the corporation **has acted** 'fraudulently, dishonestly or in bad faith' in carrying out the behaviour b) the behaviour **has been carried out for the 'purpose of** distorting or manipulating prices' in the electricity spot market. Alinta Energy considers excluding the part that reflect the characterisation and/or purpose of that behaviour, i.e. "for the purpose of", significantly changes the operation of this clause in the WEM Rules. To avoid this, we recommend the following amendment: 2.16A.2. A Market Participant must not engage in conduct in offering to supply or supplying, or in failing to offer to supply or supplying, a Market Service that: a) is false, misleading, or likely to mislead; b) is fraudulent, dishonest or in bad faith; or c) is for the purpose of distorting or manipulating ~~distorts or manipulates, or is likely to distort or manipulate,~~ prices in the Wholesale Electricity Market.

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Lower	**General Trading Obligations**	2.16A.2	The amended clauses 7.4.41 and 7.4.42 are meant to "clarify that Market Participants are not required to offer all of their accredited FCESS capacity in their Real-Time Market Submissions". However, we are uncertain how withholding this capacity would be interpreted under the general trading obligations. We recommend that these obligations clarify the situations where not offering accredited FCESS capacity should not be considered as a potential breach.
	General trading obligations	2.16A.3(a)	We support this change which is consistent with our feedback.
	Portfolio Assessment	2.16B and glossary	We support this change which is consistent with our feedback.
	Market Power Test	2.16C.3 (b) and (c)	We support this change which is consistent with our feedback.

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Highest	Market Power Test	2.16C.3 2.16D.1.	We recommend the following change to 2.16C.3: (b) maintain adequate records (that are capable of independent verification) of the methods, assumptions and cost inputs the Market Participant used to develop the prices in the Portfolio Supply Curve offered in its STEM Submissions~~, which must include, for each relevant Facility, the information referred to in clause 2.16D.1(a)(i)~~; and (c) maintain adequate records (that are capable of independent verification) of the methods and cost inputs the Market Participant used to develop the prices offered, quantities and Ramp Rate Limits in its Real-Time Market Submissions~~, which must include, for each relevant Facility, the information referred to in clause 2.16D.1(a)(i)~~. 2.16D.4. For the avoidance of doubt, 2.16C.3 does not require Market Participants to maintain records that stipulate precisely how each offer was calculated. 2.16D.1(a)(i) no longer contains a list of variable costs and so does not appear to be the correct reference for clause 2.16C.3. The amended clause 2.16D.1 instead refers to "all efficient reasonable costs". However, it would be impractical to require participants to include records for how all these costs are calculated, noting that offers can include cost inputs which a not calculated mechanistically. Non-fuel opportunity costs and how all costs are amortised are based on many uncertain market variables and human perceptions of risks. As follows we also recommend a new clause 2.16D.4 to clarify the expectation for these records. Costs that are reasonable to include are: fuel, variable operating and maintenance, regulatory costs and start up and shutdown. We support the changes to require the offer construction guideline to permit the recovery of long term take or pay fuel contracts.
Lower	Market Power Test	2.16C.5	We recommend the following changes: ~~2.16C.5. A Market Participant must not make an Irregular Price Offer that results in inefficient market outcomes.~~ We consider that this clause, and the term "Irregular Price Offer" is duplicative, noting that participants are already obliged to offer consistently with 2.16A.1 and 2.16A.2.

Highest		2.16C.6 -9. 2.13.27 2.16E.1-2	We recommend the following changes: ~~2.16C.6. The Economic Regulation Authority must investigate a potential breach of clause 2.16A.1 in accordance with clause 2.13.27 and the WEM Procedure referred to in clause 2.16D.15, and having regard to the Offer Construction Guideline, and if it considers that: (a) prices offered by a Market Participant in its Portfolio Supply Curve are inconsistent with the prices that a Market Participant without market power would offer in a profit-maximising Portfolio Supply Curve; or~~ ~~(b) prices offered by a Market Participant in its Real-Time Market Submissions are inconsistent with the prices that a Market Participant without market power would offer in a profit-maximising Real-Time Market, must determine that the prices were an Irregular Price Offer. 2.16C.7. The Economic Regulation Authority must investigate and determine, in accordance with clause 2.13.27, and the WEM Procedure specified in 2.16D.15, whether an Irregular Price Offer determined under clause 2.16C.6 has resulted in an inefficient market outcome.~~ ~~2.16C.7. The Economic Regulation Authority must investigate and determine, in accordance with clause 2.13.27, and the WEM Procedure specified in 2.16D.15, whether an Irregular Price Offer determined under clause 2.16C.6 has resulted in an inefficient market outcome.~~ These clauses duplicate 2.13.27 and in doing so, apply a different standard for investigation compared with 2.13.27. For example, it is not clear whether ERA must still apply its risk register in deciding to investigate under 2.16C.6-7, nor whether the other clauses which are triggered by 2.13.27, like the procedural fairness required under 2.15.3, would apply to these investigations. Additionally, the current drafting of 2.16C.6, 2.16C.7 and 2.13.27, would require the ERA to investigate an alleged breach of 2.16A.1 where it does not reasonably consider that the alleged breach would have caused a market outcome that warrants the regulatory effort required to investigate and address it. This would be inconsistent with the reforms objective to make regulatory effort proportional to the risk it aims to mitigate. It also contradicts 2.16E.1 which prohibits from ERA progressing an investigation where it does not result in an "inefficient market outcome". To avoid this, it would be better to augment 2.13.27, so that it applies the effects tests to general bidding obligations, rather than creating duplicative and parallel requirements for ERA to investigate new clauses 2.16C.6-9. 2.16E.1 should also be amended to clarify that ERA must not investigate unless it considers it is likely to pass the effects test, and clarify the concept of an "inefficient market outcome": 2.13.27. Subject to section 3A.12, if the Economic Regulation Authority becomes aware of an alleged breach of the WEM Rules or WEM Procedures, then:

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			(a) it must record the alleged breach; (b) subject to clause 2.13.32, and 2.16E.1, it must investigate the alleged breach in accordance with the risk rating assigned to the type of alleged breach in the WEM Procedure referred to in clause 2.15.1; (c) notwithstanding clause 2.13.27(b), subject to clause 2.13.32, it may investigate the alleged breach where the ERA considers this is reasonably required; (d) it must determine whether a breach of the WEM Rules or WEM Procedures has occurred; and (e) it must record the results of each investigation. 2.16E.1. ~~Subject to clauses 2.16C.6 and 2.16C.7,~~ the Economic Regulation Authority must not, in respect of a price offer described in clause 2.16C.4, investigate a Market Participant under clause 2.13.27, or take enforcement action under clause 2.13.36 for a breach of clause 2.16A.1, where the Economic Regulation Authority does not reasonably consider ~~has determined under clause 2.16C.7~~ that an ~~Irregular Price Offer~~ alleged breach of 2.16A.1 by the Market Participant has had material impacts on market outcomes; and that these impacts would be proportional to the regulatory effort required to investigate and address the alleged breach. ~~not resulted in an inefficient market outcome.~~ With the above changes, 2.16E.2 would only be required to the extent that ERA initially considers that an investigation is warranted under 2.16E.1 but subsequently finds that the market outcomes do not warrant proceeding with the investigation or enforcement actions: 2.16E.2. Where the Economic Regulation Authority ~~has determined that an Irregular Price Offer by a Market Participant has not resulted in an inefficient market outcome,~~ subsequently determines that the market impacts of the alleged breach do no warrant further investigation or enforcement actions, the Economic Regulation Authority must advise the Market Participant on the results of the investigation. As a less preferable alternative to the above changes, we recommend that 2.16C.6-7 are made subject to our proposed amended version of 2.16E.2. And there is not a mandatory requirement to investigate (consistent with 2.13.27).

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Lower	Market Power Test	2.16C.11	We recommend the following changes: 2.16C.11 For the avoidance of doubt, ~~nothing in these WEM Rules prohibits~~ the Economic Regulation Authority may still ~~from~~ commence~~ing~~ an investigation into an alleged breach of clause 2.16A.1, subject to 2.16E.1 and 2.13.27 if the Economic Regulation Authority was not monitoring the Market Participant's price offers at the time of the alleged breach because the Market Participant was not captured under clause 2.16C.4. As drafted, 2.16C.11 appears to make a contradictory statement that there is "nothing" in the WEM Rules to prohibit an investigation because 2.16E.1 and 2.13.27 could prohibit an investigation in these circumstances.
Lower	Guidance, WEM procedures and Consultation Framework	2.16D.6 to 2.16D.13	Alinta Energy notes that the ERA's current Compliance Framework and Strategy[1] and its Compliance Monitoring Protocol states that: The ERA's approach is aimed at encouraging compliance by Rule Participants with the Market Rules and Market Procedures with the target of achieving high levels of compliance. Under this approach the ERA will seek to: (a) assist Rule Participants to understand their obligations, noting that the responsibility for meeting compliance obligations rests with the individual participant. Alinta Energy is concerned clauses 2.16D.6 to 2.16D.13 adds unnecessary prescription to the process for seeking guidance and that by requiring the formulaic responses within set timeframes, the rules would undermine the opportunity for Market Participants and the ERA to build collaborative, transparent and good faith working relationships which are critical to compliance outcomes. Alinta Energy commends the ERA Market Compliance team for its work in supporting this culture within the WEM and suggests removing the prescription to avoid hampering opportunities to build on this in the new market.

[1] Compliance Framework and Strategy (erawa.com.au)

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Lower	Conducting a Review of a Market Price Limit	2.26.2	We recommend that 2.26.2 also note that the price ceiling should be based on the shortest feasible run of the highest cost generating unit. Noting that the bidding obligation considers the opportunity cost of fuel, and that it is proposed the limit is reviewed every three years rather than annually (like it is now), we also suggest that the fuel input be based on the maximum fuel price which may reasonably occur during the three-year period, considering the forecast supply and demand balance. As evidenced by the most recent review, the current method uses normal distributions of fuel and run times, rather than minimum run times or the maximum fuel price reasonably expected during the period, causing participants to under-recover costs in many intervals.[2]
Highest	Supplementary Essential System Service Mechanism	3.15A.2A	We strongly question the need for these benchmarks, and we are concerned they will become a de facto price limit, triggering investigations or the SESSM and duplicate the current offer requirements. We also note that determining these benchmarks will be labour intensive, complex and fraught with forecast risk – like, the current margin values process. We continue to strongly oppose the trigger for the SESSM based on efficient market outcomes, especially considering this extensive market power mitigation framework, and ERA's findings highlighting the uncertainty and revenue gaps facing new storage capacity and how new entrants in the FCESS market dramatically reduces revenue for incumbents, further undermining the incentive to invest. If retained, we recommend that the rules outline how these benchmarks should be determined.

[2] This issue is further detailed in our submission

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Lower	Real-time market submissions: Obligations and meaning	7.4.26 and 7.4.27	Alinta Energy supports the record keeping concept in principle. However, we are concerned with the requirement to be "adequate detailed records". To ensure there is balance between maintaining sufficient records to allow a proper investigation to be held and minimising compliance risk and cost, Alinta Energy considers the word "detailed" should be deleted. This drafting has been removed in other clauses, so should be removed here as well for consistency. The level of detail required should then be detailed in a WEM procedure (which could be the same procedure referred to in clause 2.16C.3). This approach upholds the desire for the WEM rules to set the objectives and the subsidiary documents to contain the detail. Additionally, we recommend that the requirement for participants to note the time of a change in circumstances impacting an offer, and the time they became aware is excessively burdensome for a trader and operators in a real time market. If any part of this requirement is retained, we recommend that only the estimated time of the change should remain. It can be inferred that the time the offer was submitted was close to the time the trader became aware. It can also be problematic noting that a trader can be aware of a change but not sufficiently certain of it to update offers.
Highest	ESS offers		Per our submission on the market power mitigation strategy paper, we remain concerned about the planned approach to ESS pricing and ESS uplift payments and the uncertainty and complications it could impose on constructing ESS and energy offers. Participants would not be able to cooptimise their offers but must rely on uncertain estimated uplift payments in pricing their capacity. We consider that this creates a compliance risk and a risk of under-recovery. We recommend that rules clarify whether ESS offers may include energy opportunity costs.