

# 2013 Energy Price Limits Decision

11 June 2013

**Economic Regulation Authority**

WESTERN AUSTRALIA

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## DECISION

1. Pursuant to clause 2.26 of the *Wholesale Electricity Market Rules (Market Rules)*, the Economic Regulation Authority (**Authority**) approves the revised value for the Maximum Short Term Energy Market (**STEM**) Price of \$305/MWh.
2. Pursuant to clause 2.26 of the Market Rules, the Authority approves the price components for the Alternative Maximum STEM Price:  
  
\$67.33/MWh + 19.719 multiplied by the delivered distillate fuel cost in \$/GJ
3. In accordance with clause 6.20.11 of the Market Rules, the approved revised value for the Maximum STEM Price and the Alternative Maximum STEM Price will apply with effect from the time specified in a notice to be published on the Independent Market Operator's (**IMO**) website.

## REASONS

### Background

4. Clause 6.20.6 of the Market Rules requires the IMO to annually review the appropriateness of the value of the Energy Price Limits. Clause 6.20.7 states that in conducting the review, the IMO may propose revised values for the Maximum STEM Price and the Alternative Maximum STEM Price. If it does propose such revised values, the IMO must use the applicable methodology set out in clause 6.20.7(b) of the Market Rules.
5. Where, as a result of its review, the IMO has proposed a revised value for the Maximum STEM Price and/or the Alternative Maximum STEM Price, the IMO is required to prepare a Draft Report describing how it arrived at a proposed revised value of an Energy Price Limit. The IMO must publish the report on the Market Website<sup>1</sup> and advertise the report in newspapers widely published in Western Australia, and request submissions from all sectors of the Western Australian energy industry, including end-users, within six weeks of the date of publication. After considering the submissions on the Draft Report, the IMO must propose a final revised value for any proposed change to an Energy Price Limit and submit those values and its Final Report, including submissions received on the Draft Report, to the Authority for approval.
6. The Market Rules require the Authority to review the Final Report provided by the IMO, including all submissions received by the IMO in the preparation of the report, and to make a decision as to whether or not to approve the revised value for any value comprising the Energy Price Limits.<sup>2</sup>
7. In making its decision as to whether or not to approve any proposed change to an Energy Price Limit, the Authority must only consider:<sup>3</sup>

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<sup>1</sup> Pursuant to the *Electricity Industry (Wholesale Electricity Market) Regulations 2004*, the IMO is required to maintain an internet website for the purpose of publishing and releasing information to Market Participants.

<sup>2</sup> Pursuant to clause 2.26.1(a) and (b) of the Market Rules.

<sup>3</sup> Pursuant to clause 2.26.1(c) of the Market Rules.

- whether the revised value for the Energy Price Limit proposed by the IMO reasonably reflects the application of the method and guiding principles for calculating the Energy Price Limits described in clause 6.20 of the Market Rules; and
- whether the IMO has carried out an adequate public consultation process.

## The IMO's process

8. The IMO's annual Energy Price Limits review uses information on gas prices in Western Australia as an input variable. The IMO engaged ACIL Tasman to assist in undertaking a review of gas prices in Western Australia.<sup>4</sup> ACIL Tasman's Draft Report on gas prices in Western Australia was published for consultation on the IMO's website on 12 February 2013. In response to the draft report, no submissions were received by the IMO. Following the public consultation period, the IMO published its Final Report on the 2013 review of gas prices in the WEM and ACIL Tasman's Final Report on gas prices in Western Australia on 6 March 2013. The outcomes of this review were used as inputs in the 2013 Energy Price Limits review.
9. The IMO engaged Sinclair Knight Merz / McLennan Magasanik Associates (**SKM MMA**) to assist it in undertaking the 2013 Energy Price Limits review. SKM MMA provided the IMO with its Draft Report on the review of the 2013 Energy Price Limits on 19 March 2013, which was published for consultation on the IMO's website.<sup>5</sup> The consultation period closed on 3 May 2013. The IMO received one submission from Community Electricity.
10. On 17 May 2013 the IMO provided the Authority with its Final Report, together with SKM MMA's Final Report on the review of the Energy Price Limits.
11. The IMO subsequently updated the revised Loss Factors determined by Western Power for the 2013/14 financial year and the final values of the Energy Price Limits were provided to the Authority on 10 June 2013.

## The Authority's assessment

12. The Authority has reviewed ACIL Tasman's Draft and Final Reports on gas prices in Western Australia. The Authority has also reviewed SKM MMA's Draft and Final Report and the IMO's Final Report on the review of the Energy Price Limits.
13. The Authority considers that the IMO's proposed revised values for the Energy Price Limits reasonably reflect the application of the methodology, as defined in clause 6.20.7(b) of the Market Rules.
14. The Authority is satisfied that the IMO has carried out an adequate public consultation process. The IMO published the Draft Report prepared by SKM MMA, describing how it arrived at the proposed revised values of the Maximum STEM Price and the Alternative Maximum STEM Price on the Market Website, accompanied with an invitation for submissions. The IMO also advertised a notice in newspapers widely

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<sup>4</sup> See IMO website, Gas prices in Western Australia 2013-14 Review of inputs to the Wholesale Electricity Market, [http://www.imowa.com.au/f7054,3737632/Gas\\_Prices\\_in\\_WA\\_2013-14\\_Final\\_Report.pdf](http://www.imowa.com.au/f7054,3737632/Gas_Prices_in_WA_2013-14_Final_Report.pdf)

<sup>5</sup> See IMO website, Energy Price Limits for the Wholesale Electricity Market in Western Australia from July 2013, [http://www.imowa.com.au/f7185,3719790/SKM\\_MMA\\_Draft\\_Report\\_2013\\_Energy\\_Price\\_Limits\\_Review.pdf](http://www.imowa.com.au/f7185,3719790/SKM_MMA_Draft_Report_2013_Energy_Price_Limits_Review.pdf)

distributed in Western Australia inviting submissions from all sectors of the Western Australian energy industry, including end-users.

15. The Authority notes the IMO's consideration for making amendments in the Market Rules to:
  - more transparently describe the current probabilistic methodology used for the Energy Price Limit review.
  - streamline the annual review process for the determination of the Energy Price Limits; and
  - extend the IMO's powers to request actual operational data from Market Participants, to provide more accurate input to the modelling process, as part of the Energy Price Limits review.
16. As stated in the Authority's 2011 and 2012 Energy Price Limits decision, the Authority was of the view that there is an inconsistency between clause 6.20.7(a) and 6.20.7(b) of the Market Rules. Clause 6.20.7(a) refers to the Maximum STEM Price being based on the IMO's estimate of the **short run marginal cost** of the highest cost generating works in the South West Interconnected System fuelled by natural gas. It is to be calculated using the formula in clause 6.20.7(b), which refers to the Risk Margin used to calculate the Maximum STEM Price being a measure of uncertainty in the assessment of the mean **short run average cost** for a 40 MW open cycle gas turbine generating station. The Authority considers that this matter should also be subject to the IMO's review.
17. The methodology for calculating the Alternative Maximum STEM Price is provided in clause 6.20.3(b) of the Market Rules, which comprises a non-fuel and fuel component that is based on delivered cost of the Singapore Gas Oil (0.5% sulphur) price. For the fuel component of the Alternative Maximum STEM Price, SKM MMA applied a ratio to convert the delivered distillate fuel cost in \$/GJ into \$/MWh. The delivered distillate fuel cost in \$/GJ to be converted comprises the cost of transport and excise, which is a fixed cost. The Authority is of the view that a ratio should not be applied to the transport and excise cost components as these are fixed and are already in \$/MWh. Instead, these cost components should be added on after the other fuel cost components have been converted to \$/MWh in order to derive the fuel component of the Alternative Maximum STEM Price. The Authority considers that this matter should be subject to the IMO's review.
18. Pursuant to clause 2.26.3 of the Market Rules, the Authority must review the methodology for setting the Maximum Reserve Capacity Price (**MRCP**) and Energy Price Limits not later than the fifth anniversary of the first Reserve Capacity Cycle and, subsequently, not later than the fifth anniversary of the completion of the preceding review. That is, the Authority must review the methodology for setting the MRCP and Energy Price Limits not later than 1 October 2013. The Authority has commenced this review process and expects to conclude this review within the timeframe stipulated in the Market Rules.
19. The Authority notes that in past Energy Price Limits Decisions, the Authority had approved a single revised value for the Alternative Maximum STEM Price. However, as the Alternative Maximum STEM Price is revised every month according to changes in the Singapore Gas Oil (0.5% sulphur) price as provided in clause 6.20.3(b) of the Market Rules, the Authority considers it is more appropriate to approve the price

components for the Alternative Maximum STEM Price rather than a single revised value.

## Conclusion

20. On the basis of the above information, the Authority is satisfied that:

- the proposed values for the Energy Price Limits by the IMO reasonably reflect the application of the method and guiding principles for calculating the Energy Price Limits; and
- the IMO has carried out an adequate public consultation process.