

Decision on 2012 Energy Price Limits

Submitted by the Independent Market Operator

22 June 2012

Economic Regulation Authority

WESTERN AUSTRALIA

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DECISION

- 1 The Economic Regulation Authority (**Authority**) approves the revised value for the Maximum Short Term Energy Market (**STEM**) Price of \$323/MWh, and the Alternative Maximum STEM Price of \$547/MWh pursuant to clause 2.26 of the *Wholesale Electricity Market Rules* (**Market Rules**).
- 2 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, which will be 1 July 2012 in alignment with the introduction of carbon pricing.

REASONS

Background

- 3 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.
- 4 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 Website¹ 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.
- 5 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.²
- 6 In making its decision as to whether or not to approve any proposed change to an Energy Price Limit, the Authority must only consider:³

¹ 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.

² Pursuant to clause 2.26.1(a) and (b) of the Market Rules.

³ 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

- 7 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.⁴ The outcomes of this review were used as inputs in the 2012 Energy Price Limits review.
- 8 The IMO engaged Sinclair Knight Merz / McLennan Magasanik Associates (**SKM MMA**) to assist it in undertaking the 2012 Energy Price Limits review. SKM MMA provided the IMO with its Draft Report on the review of the 2012 Energy Price Limits on 17 April 2012, which was published for consultation on the IMO's website.⁵ The consultation period closed on 30 May 2012. The IMO did not receive any submissions during the public consultation period.
- 9 The IMO invited Rule Participants to attend a workshop on the Draft Report, which was held on 16 May 2012. This workshop was attended by representatives from SKM MMA, Eureka Electricity, Synergy, the IMO and the Authority's Secretariat.⁶
- 10 On 6 June 2012 the IMO provided the Authority with its Final Report, together with SKM MMA's Final Report on the review of the Energy Price Limits.

The Authority's assessment

- 11 The Authority has reviewed SKM MMA's Draft and Final Report and the IMO's Final Report on the review of the Energy Price Limits.
- 12 The Authority notes that SKM MMA's Final Report was prepared before the revised loss factors for the 2012/13 financial year became available to the IMO. The IMO did not ask SKM MMA to update its Final Report to reflect the new loss factor for the Pinjar unit used in calculating the Energy Price Limits, given the small impact of the change and the timeframes required to meet the 1 July 2012 implementation date. The Authority notes that the IMO has updated its Final Report to reflect the new loss factor for the Pinjar unit used in calculating the Energy Price Limits.

⁴ See IMO website, Gas prices in Western Australia 2012/13 Review of inputs to the Wholesale Energy Market, http://www.imowa.com.au/f5595,2142874/Gas_Prices_in_WA_2012-13_Final_Report_FINAL.pdf

⁵ See IMO website, Energy Price Limits for the Wholesale Electricity Market in Western Australia from October 2011,http://www.imowa.com.au/f5789,2194905/SKM_MMA_Draft_Report_2012_Energy_Price_Limits_Review.pdf

⁶ See IMO website, 2012 Energy Price Limits Review Workshop Minutes,http://www.imowa.com.au/f5789,2308387/Minutes_2012_Energy_Price_Limits_Review_Workshop_FINAL.pdf

- 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 distributed in Western Australia inviting submissions from all sectors of the Western Australian energy industry, including end-users.
- 15 The Authority is in support of the IMO making amendments in the Market Rules to more transparently describe the current probabilistic methodology used for the Energy Price Limit review.
- 16 The Authority is in support of the IMO's consideration to streamline the annual review process for the determination of the Energy Price Limits.
- 17 The Authority is also in support of amending the Market Rules to 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.
- 18 As stated in the Authority's 2011 Energy Price Limits decision, it is of the view that there is an inconsistency between clause 6.20.7(a) and 6.20.7(b) of the Market Rules, with respect to applying the short run marginal cost and short run average cost, respectively, in calculating the Maximum STEM Price. Clause 6.20.7(a) of the Market Rules 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, and is to be calculated using the formula in paragraph (b) of clause 6.20.7 of the Market Rules. Clause 6.20.7(b) of the Market Rules 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.
- 19 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 intends to conduct this review within the timeframe stipulated in the Market Rules.

Conclusion

- 20 On the basis of this information, the Authority is satisfied that:
- the proposed values for the Energy Price Limits set out in the IMO Final Report 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.