

13 October 2025

Steve Edwell
Chair
Economic Regulation Authority
L4, Albert Facey House
469 Wellington Street, Perth WA 6000

Via email: publicsubmissions@erawa.com.au

Dear Mr Edwell

RE: Electricity Generation and Retail Corporation Regulatory Scheme 2025 effectiveness review

Thank you for the opportunity to comment on the effectiveness of the Electricity Generation and Retail Corporation (**EGRC**) Regulatory Scheme.

Standard and customised products, as currently designed, are not well suited to meet the evolving needs of the power system. We consider that the existing standard products are no longer fit for purpose in a high-renewables market. However, they could evolve to form the basis of a cap contract product that enables peaking generators to smooth revenue flows and allows renewable generators to manage exposure to price volatility. In particular, expanding standard products to include standardised and tradable derivative instruments would allow participants who cannot physically mitigate price risk to effectively hedge their financial exposure.

As the Economic Regulation Authority (**ERA**) has identified, as renewable penetration increases, price volatility increases and there is presently no robust path for many consumers or renewable generators to manage this risk effectively.

To facilitate discussion on how standard products could evolve, we have prepared a separate discussion paper at **Attachment 1**. The paper sets out the case for introducing a cap contract derivative product in the WEM. A cap product would support peaking plant to secure long-term revenues that are not dependent on volatile spot prices, and it would allow renewable generators to hedge financial exposure to price spikes. Our answers to the Discussion Paper questions are framed with this objective in mind.

We also note the alignment with the Nelson Review's findings on the need to deepen derivatives markets, to improve liquidity through basic market-making, and to broaden contract types beyond simple firming of electrons to instruments that hedge price volatility and duration risk. These themes support an evolution of the standard product regime toward fungible, tradable financial products that deliver better risk transfer, more transparent price signals, and stronger investment certainty over longer tenors.

We have not responded to all points in the Discussion Paper. This is because we do not use standard products in our portfolio. We have responded where appropriate and where our experience can assist the ERA.

Response to questions

Q1. What role do standard products have in your hedging portfolio?

Standard Products are designed around the purchase and sale of electrons. As a fully bilaterally contracted semi-scheduled generator, we are unable to effectively use the existing standard products provided in the EGRC scheme to hedge our portfolio.

As these products are structured and traded in fixed quantity blocks rather than as standardised price-based financial derivatives, they do not align with the variable output profile of renewable generators or the price risk we face. While CfD-style bilateral PPAs can provide project-specific hedges, they are inherently bespoke and illiquid, offering no broader market benefit or price transparency. Given the highly bilaterally contracted nature of the WEM, we expect that other large generators and customers face similar limitations, reinforcing the need for a standardised financial derivative product to enable efficient, transparent risk management across the market.

Q2. Does the market need standard products? Please provide reasons.

The WEM needs strong market power mitigation tools. The ERA has signalled that standard products are the primary tool within that scheme. We support retaining an effective mechanism that mitigates the market power of dominant parties, noting that product design and market-making settings should also promote liquidity and transparency. In our view, a standardised financial derivative product is essential to achieving a mature and robust market structure in which multiple independent generators can competitively sell to a limited pool of customers. Without such a financial product, participants must rely on bespoke bilateral arrangements or physical hedges, which limit competition and increase costs. If full retail contestability is not pursued, the introduction of a standardised financial derivative becomes even more critical to ensure that customers and independent generators have access to transparent, tradeable instruments to manage price volatility and support efficient investment and contracting outcomes.

Q3. Has the importance of standard products for your business changed since October 2023? If so, how?

Not applicable.

Q4. Have recent price outcomes affected your inclination to access standard products?

Not applicable.

Q5. How important are standard product prices in determining customer pricing in your business?

While we do not use standard products, they contribute to price discovery and provide useful transparency and signals for customers seeking long-term power purchase agreements.

Q6. What would the impact on your business have been, if any, in the absence of the standard products offered by Synergy?

No direct impact.

Q7. What considerations impact your decision on whether to trade in standard products, for example price, terms, and conditions?

Not applicable.

Q8. Do you consider the current buy-sell spread should change? Please provide reasons.

Not applicable.

Q9. How can the scheme address Synergy’s potential to exercise market power on either the buy or sell side and remain agnostic to Synergy’s net position?

Not applicable.

Q10. Does the WEM need separate hedging and forecasting services? If so, how might such mechanisms operate?

Hedging and forecasting perform separate, equally important functions. The separation of physical delivery from financial hedging can be achieved through derivative contracts. To address the small and illiquid nature of the WEM, two elements are needed:

1. a basic market-making function to ensure continuous, posted bids and offers for agreed products and tenors, and
2. products that are genuinely fungible and tradable, so participants can risk-manage efficiently, unwind positions when needed.

Q11. What considerations impact your decision on whether to trade in standard products, for example price, terms, and conditions?

Not applicable.

Q12. What features do you consider warranted in a standard product regime?

As noted above, the regime should evolve from a mechanism that firms electrons to one that enables market participants to mitigate price volatility risk. This points to a catalogue that includes cap products and other standardised derivatives with clear specifications, transparent settlement, and basic market-making to support liquidity.

Q13. Should the definition of “peak period” be aligned with the actual peak periods in the WEM?

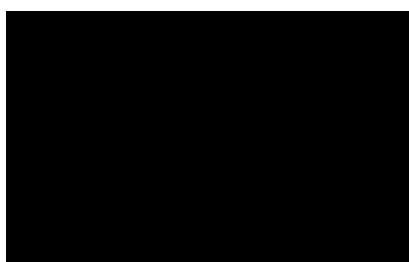
Not applicable.

Q14. Should force majeure provisions be altered? If so, why and how?

Not applicable.

If you have any questions or would like to discuss any part of our response, please do not hesitate to contact Jake Flynn via email jake.flynn@collgar.com.au. We look forward to engaging with the ERA further on the points raised in the separate Discussion Paper at **Appendix 1**.

Kind regards





Attachment 1: Discussion Paper

Date 13 October 2025

To Economic Regulation Authority

From Collgar Renewables

Subject Case for Introducing a Cap Contract Derivative Product into Western Australia's Wholesale Electricity Market

1 Executive summary

Western Australia's Wholesale Electricity Market (**WEM**) is undergoing structural change as it shifts away from vertically integrated bilateral agreements towards a more transparent, competitive and renewable based framework. As the energy transition progresses and the share of renewable generators grows, market customers face new financial exposures. This exposure is, in part due to inherent fuel constraints of renewable generation increasing the potential for market volatility.

To support a stable investment environment and enable independent power producers (**IPPs**) to offer firmed renewable products, this memo proposes the development of a deeper financial market to overlay the physical market, via the introduction of a Cap Contract derivative in the WEM. Such a product would allow renewable generators and market customers to hedge high-price periods, de-risk investments in flexible generation, and optimise capital deployment across the system.

These recommendations are strongly aligned with the findings of the 2025 NEM Wholesale Market Settings Review (**Nelson Review**), which calls for targeted reforms to enhance liquidity in the short-to medium-term derivative market (Recommendations 6 and 7) and unlock long-term investment in new energy services (Recommendations 8 and 9).

Applying these insights to the WEM context, Cap Contracts offer a practical tool to support both objectives.

2 Problem Statement

2.1 Transition to CfD based procurement

Although the WEM has historically been mostly bilaterally contracted, it is moving towards centralised and Contract for Difference (**CfD**)-based procurement mechanisms for both capacity and energy. This change is displacing traditional bespoke bilateral arrangements.

2.2 Increased exposure to renewable volatility and price risk mitigation

As renewable penetration rises, so too does exposure to weather-driven pricing volatility. Customers now face increased risk during periods of correlated low wind and solar output. Without a financial mechanism to manage this risk, each supplier must develop its own physical hedge, typically via



over-investment in Battery Electric Storage System (**BESS**) or gas generation. This leads to inefficient investment decisions as there is no mechanism to pool infrequently used peaking assets, driving up system wide costs and reducing overall market efficiency.

In the absence of a liquid financial product, such as a cap contract, participants in the WEM have very limited means of hedging against pricing risk. Unlike traditional thermal generators, renewable facilities cannot easily adjust their output to align with periods of high demand or price volatility. Without a financial hedge, market customers are exposed to sharp and unpredictable cost increases, which undermines their ability to manage budgets and enter long term procurement arrangements with confidence.

If a cap product is not developed, renewable generators will be forced to pursue physical hedging solutions, such as over-building gas-fired generation or over-development of large-scale battery storage to provide market customers with de-risked Power Purchase Agreements (**PPA**). This approach is both capital intensive and inefficient as it requires unnecessary duplication of infrastructure rather than leveraging a financial market mechanism.

Industry understands that additional gas-fired generation may be part of the solution to the looming energy shortfall following coal retirement. While this approach presents its own unique challenges around gas availability and pricing, it is important that any future gas-fired generation is utilised efficiently to ensure an appropriate return on investment. A cap contract mechanism could support this by providing an additional revenue stream for these generators, enabling them to better manage fuel-cost exposure while contributing to system reliability during periods of high demand and price volatility.

2.3 Inadequacy of current products

Synergy offers Standard Products which provide a transparent and regulated wholesale pricing mechanism that enables customers to purchase set quantities at pre-defined prices. However, these products are limited in scope, illiquid, and primarily serve as indicative benchmarks rather than genuine hedging tools. Customised products offered by Synergy are opaque and not structured to efficiently allocate risk or encourage new firming investment. The result is a thin market with limited pricing signals for peaking capacity.

Standard Products negotiated with Synergy are bespoke bilateral terms. They are not fungible and can not be easily traded or compared. Contract terms including size, shape and settlement vary from contract to contract, there is little if any, secondary trading and weak price discovery. Rather than change the current standard products framework, we support adding a simple Cap Contract as a true, standardised product. A Cap Contract would be fungible, easier to value and open the door to more counterparties, which can help a deeper and more liquid market develop.

3 Cap Contracts Solution

Design overview and jurisdictional comparisons.

In the National Electricity Market (**NEM**), Cap contracts are financial derivatives widely traded on the ASX electricity futures market. The Australian Energy Regulator explains that a cap contract sets a strike price (commonly \$300/MWh, but it could be any value); if the spot price exceeds this strike, the seller (typically a generator) must pay the buyer (usually a retailer) the difference, while the buyer pays an upfront premium to the seller. Because they are option contracts, the buyer is not obliged to call upon the contract but pays a premium for the right to limit exposure.



The Nelson Review is currently under consultation with several recommendations to strengthen these products. Recommendations include establishing an 'always on' market making obligation, to increase market depth and liquidity; and ensuring there is sufficient market information to support longer term derivatives liquidity and price discovery.

The use of derivative products is reasonably common in other jurisdictions including New Zealand Electricity Market, Ireland and North Ireland's Single Electricity Market, Japan's Power Exchange, various North American exchanges and the European Energy Exchange.

3.1 System benefits

Cap contracts provide a cost-effective means of sharing peak price risk across the electricity market. They allow renewable generators to manage volatility exposure without over investing in redundant firming assets. By avoiding unnecessary capital duplication, they may help contain Capacity Credit cost and ensure system reliability through a more efficient use of existing flexible resources.

In parallel, these contracts create a direct incentive for investment in new dispatchable capacity. Transparent price signals support competition, improve retail product innovation and give customers better tools to hedge exposure. This aligns with the Nelson Review recommendations that seek to enhance liquidity and bring forward investment.

A well designed, standardised WEM cap contract would convert short-term price risk into predictable cashflows. This gives buyers and renewable developers bankable revenue certainty that supports financial investment decisions. It aligns with the Nelson Review's long-term direction to strengthen derivatives and market making so private capital can finance firmed renewables over longer tenors, and it complements Energy Policy WA's (**EPWA**) WEM Investment Certainty work program by providing transparent, scalable hedge that reduces reliance on costly physical overbuild to de-risk PPAs.

Worked example and benefits.

To illustrate how a cap product could function in the WEM, consider a 1 MW renewable generator (wind or solar farm) contracting with a private peaking plant for a quarterly \$250/MWh cap. Key assumptions mirror the NEM but adapt to WEM price dynamics:

1. Contract terms: The renewable generator (**buyer**) agrees to pay the peaking generator (**seller**) a premium of \$15 for each MW of unit volume required by the buyer across the quarter. The contract covers a *volume* of 1 MW for all half hour intervals in the quarter.
2. The strike price is \$250/MWh.
3. During low price periods: When the spot price is below \$250/MWh, the seller keeps the premium and has no obligation. If the seller chooses to generate, it sells into the Real-Time Market normally.
4. During price spikes: Suppose 40 hours in the quarter experience spot prices above the strike, with an average price of \$400/MWh. The seller must pay the buyer the difference (i.e., \$400 – \$250 = \$150/MWh for 1 MW over 40 hours = \$6 000). This payout offsets the buyer's exposure to high prices.
5. Revenue to seller: The seller receives the premium: \$15/MWh × 1 MW × 24 hours/day × 90 days ≈ \$32 400. Subtracting the payout (\$6 000) leaves \$26 400.



6. Benefits for the Peaking Facility: For the seller this revenue helps finance capital and fixed costs.
7. Benefit to renewable generator: The generator caps its exposure at \$250/MWh, ensuring predictable revenue and the ability to bid aggressively in CfDs or retail contracts. Without the cap, the generator would have paid \$400/MWh during the 40 hours, costing \$16 000; under the cap it pays the seller the premium (\$32 400) minus the payout (\$6 000) or net \$26 400. Should the wholesale price sit at the WEM Energy Offer Price Ceiling of \$1000/MWh across those 40 hours over the quarter, a cap contract could mitigate up to \$30,000 of spot market price risk for a renewable generator (i.e. $\$1000 - \$250 = \$750 \times 40 = \$30,000$). Such a cap contract product mitigates unpredictable extreme costs risk that can threaten project bankability.
8. Benefits for Market Customers: The introduction of a cap contract product in the WEM would provide Market Customers with an effective hedge against extreme price volatility, while also increasing the efficiency and competitiveness of the Real-Time Market due to increased renewable and peaking-facility investment.

This simplified example shows how a cap contract transfers scarcity revenue from the renewable project to a peaking provider. By pooling risk across many generators and retailers, the market can deliver a stable revenue stream to flexible assets and mitigate price shocks for customers.

4 Implementation Considerations

4.1 Regulatory and market structure requirements

To succeed, a WEM cap contract market must be underpinned by legislative and regulatory reforms.

As in the NEM, centralised clearing and margining should be instituted to manage counterparty credit risk. The Economic Regulation Authority could designate one or more market makers with obligations to quote buys sell spreads. Unlike the present standard products, multiple licensed participants (e.g., Synergy, Alinta Energy, independent generators and large retailers) could be authorised to trade caps, improving liquidity and price discovery. Similar Market Maker obligations have been recommended by the Nelson Review in the NEM to enhance liquidity in the derivatives pool.

Several small electricity markets comparable in scale to the WEM successfully support standardised cap contract products. For example, New Zealand's market trades exchange-listed \$300/MWh electricity caps and options on ASX24 with active market-making obligations, while Singapore's Energy Market Authority facilitates bilateral and exchange-cleared cap-style hedges to manage scarcity pricing risk.

Caps should be designed to complement CfD PPAs rather than duplicate them. CfDs provide revenue certainty for capacity investment; cap contracts provide short-term price hedging for energy. Contracts should be standardised for specific periods (quarters or years) and volumes to facilitate trading. Prices should be published to provide reference curves, similar to the role of standard products but with true hedging value.

Various legislative instruments may need amendments to permit financial derivatives trading by multiple parties and to clarify the interaction with prudential requirements. Given the typical lead time for rule changes, reforms should commence immediately so the market is operational within 3–5 years



4.2 Feasibility of Cap Products in the WEM

The WEM is sufficiently large to support a standardised cap product, particularly with basic market-making arrangements. EPWA's WEM Investment Certainty work already targets stronger, bankable contracting setting via 10-year Reserve Capacity Price (**RCP**) guarantees and sharpening of the RCP curve. A cap contract would complement these measures. The Nelson Review underscores the need for deeper derivatives and market making to keep risk managed by market participants, and unlock private investment over longer tenors.

A relevant peer example is New Zealand, a smaller and similarly concentrated market that sustains exchange-traded electricity futures and options on ASX24 with active regularly support and published volumes. New Zealand demonstrates that meaningful liquidity can be achieved at modest scale when products are standardised and transparently supported.

4.3 Timing

With renewable generation forecast to materially increase by 2030, the need for scalable and liquid risk management tools is growing. Cap Contracts offer a low-cost, proven mechanism to share peak risk and enable firm product innovation. Without such tools, investment may stall, and customer risk may increase. Legislative support and implementation planning should commence immediately to enable deployment by as soon as practicable.

The proposal also complements NEM Review Recommendations 8 and 9, which highlight the need to create investment pathways and flexible contracting options to bring forward new dispatchable and renewable capacity.

5 Conclusion and recommendations

Introducing a cap contract derivative market in the WEM is a prudent, efficient response to the twin challenges of increasing renewable penetration and the shift to CfD PPAs. The cap product would provide a transparent, liquid hedge against price volatility, incentivise private investment in flexible peaking capacity, and reduce the need for each renewable generator to finance its own battery or gas turbine.

Evidence from the ERA's effectiveness review shows that current standard products are limited in volume and mainly provide price signals, while bespoke products are illiquid and hinder new entrants. *Dunkelflaute* events are likely to occur more often as renewable penetration increases and the WEM becomes more reliant on CfD-backed PPAs. Cap contracts, successfully used in the NEM and New Zealand, offer a proven solution to these challenges.

We therefore recommend that the ERA, in coordination with the Energy Policy WA and AEMO, commence work immediately to design and implement a WEM cap contract market. This should include legislative amendments to allow trading of standardised cap derivatives, the establishment of market maker obligations, and a pilot programme to build participant capability. Doing so within the next 3–5 years will ensure that the SWIS continues to deliver reliable, affordable electricity through the energy transition.

