

EUAA Meeting with the Australian Energy Regulator / Australian Competition and Consumer Commission

Issues Paper –

High Spot Price Events in the NEM in Early 2008, Transmission
Constraints, and Implications for Market Efficiency and Competition

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Introduction

In January and February 2008, a number of volatile pricing events have been evident for significant periods in the NEM but especially in South Australia and Queensland.

These are reflected in the monthly average spot prices for these regions of above \$120/MWh for SA in both January and February and \$131/MWh for QLD in February. The most sustained events occurred on 10 January and 18 February in SA and on 22/23 February in QLD. These events have been significant in the historical price context of the NEM, and due to their sustained nature have resulted in the cumulative prices reaching very close proximity to the weekly cumulative threshold level of \$150,000 and thus, nearly triggering administered pricing by NEMMCO.

If these high prices persist, there will be serious flow on effects to prices that large end users pay. There is already some indication that recent volatility has offset some softening in prices in the NEM in the early part of this year (following the very high prices seen during 2007), particularly for contracts in regions affected by spot market volatility. Recent indications are that since mid February, forward prices in the wholesale traded flat load contracts for the calendar 2009 have increased by \$3/MWh in NSW, \$5/MWh in Victoria, \$6/MWh in QLD and \$10/MWh in SA. In addition, EUAA is presently undertaking a survey of its members and results to date, plus other interaction with our members confirms that those who are presenting recontracting for energy supply are facing price increases of 50 % (on average) over current prices, and continue to report a difficult contracting environment and concerns of diminished retailer interest.

The recent price episodes also re-invoke our previously expressed concerns about:

- The bidding and rebidding Rules in the NEM, including the 'good faith' provisions;
- The significant market price impacts of interconnector constraints; and
- The existence and use of market power by some generators.

1. High Spot Price Events in January/February 2008

1.1. Events in South Australia

With respect to pricing events in SA above \$5,000/MWh, we are aware that the AER has produced a report, indicating that on both days noted above AGL offered 80 per cent of Torrens Island's capacity above \$9,000/MWh, or close to the price cap, setting the price at \$10,000/MWh. The report identifies rebidding behaviour by AGL's Torrens Island plant on several occasions, including 600 MW rebid above \$9,000/MWh on 18 February. All the capacity of Angaston generators, owned by Infratil, was priced at the maximum cap on 18 February. The report also indicates significant amounts of capacity priced above \$5,000/MWh and capacity not presented to the market between 75-100% of summer rating levels by AGL and Infratil during the high priced days. Imports from Victoria were significantly lower than historic levels, as a result of the SA and VIC transmission providers revising the limits on the Heywood connector from 500 MW to 460 MW by SP Ausnet in 2003, and 460 to 360

MW by Electranet in December 2007. These revisions have reduced import limits into SA by 140 MW or 28 per cent since 2003.

The EUAA has access to *NEM Review* which allows us to graph actual and available generation with reference to pool price and demand. We produced analysis for significant plant in SA, and noted significant variation in generation to available levels was evident for AGL and TRUenergy plant on 18 February (**See Attachment A**). Similar generator offerings by these entities were observed on 10 January.

1.2. Events in Queensland

The pricing events in QLD on 22/23 February appear to present some similar issues with respect to generator offerings and transmission availability. We are aware that on each of the days, prices reached above \$5,000/MWh for sustained periods with energy prices unaffected in other regions, and approximately 2,000 MW of available generation (10,000 MW) was offered at prices above \$7,000/MWh. We are also aware of significant variations between generation and declared available generation by Tarong Energy (**See Attachment B**), and concerned about some aspects of apparent discrepancies between available generation and despatched generation, in view of outages on both days affecting energy flow from NSW. This is despite the fact that Tarong capacity of 1,000 MW mothballed due to the drought had recently been returned to the market.

On 22 February the high prices in QLD coincided with a period where an unplanned outage of TransGrid's Lismore Static Var Compensator (SVC) restricted interconnector supply from NSW to 165 MW on QNI and 30 MW on Terranora. We are aware that Tarong was setting prices for more than 20 % of the day and that all such prices were in excess of \$1,000/MWh. It is also noteworthy that those elements of Tarong's capacity recently returned to the market were apparently uncontracted and that it was therefore in a position to potentially benefit handsomely from high spot prices.

On 23 February, transfer capacity from NSW was restricted to 200 MW on QNI to prevent voltage issues with Kogan Creek, and the Terranorra interconnector was flowing south to manage a planned outage on lines in NSW.

For prices in Queensland more generally over the period November 2007 to March 2008 (ie not specific to price spikes in February), the EUAA is also reliably informed that high prices have not correlated with a tightening supply situation. Analysis provided to us has indicated:

- Five minute dispatch prices have remained under \$1,000/MWh for 99.6 per cent of the time during the Nov 07 – Mar 08 period. In the 0.4 per cent of the time that prices rose above the \$1,000/MWh mark, NSW generators were limited in their ability to supply the market as the QNI was constrained; and
- A measure of available generation relative to instantaneous demand within the State, indicates that QLD had up to 30 per cent of available capacity idle when prices reached near the market cap.

2. EUAA Concerns

As highlighted by the AER's work, we are particularly concerned about these practices of parking capacity at maximum allowable prices at times of peak demand, and significant economic withholding of capacity, as principal contributors to the price spikes. The events have also highlighted issues with scarcity in transmission resources presenting additional opportunity for generators to drive up prices by taking advantage of limited interstate capacity sources. The ability of the Rules to guard against this behaviour, we believe, is a legitimate concern and that the AER should be considering this matter. The behaviour by AGL, described to us by some market participants as "blatant", also raises questions about market power issues with the approved transferral of TIPS from TRUenergy. Concerns about the market power that would transfer to AGL through the deal were raised by us in submissions to the ACCC when it was considering the matter. We were disappointed that the ACCC saw fit to approve this deal, in view of our market power concerns.

An interim report released by TransGrid and Powerlink for market consultation indicates that under the AER's Regulatory Test, a potential upgrade of the QNI would not be justified until 2015. The EUAA is concerned that this assessment reflects that the test, as it is presently applied, insufficiently takes account of broader customer benefits of greater interconnection. We are concerned that the Regulatory Test does not give due regard to energy infrastructure being a very significant part of the economy. We previously argued that past experiences have shown that the current regime for approving network investment has failed to deliver a sufficiently interconnected transmission grid to the benefit of end users, due to the treatment of long term consumer benefit (relative to producer benefit) in the test, eg in our submission to the Energy Reform Implementation Group in 2006 and various submissions on the Regulatory Test over many years.

The EUAA also harbours concerns that, in addition to national market-wide benefits of transmission development being forgone from the 'hurdle' of the Regulatory Test, transmission providers due to disincentives, place different priorities on inter-regional and intra-regional infrastructure development, favouring the latter as their assets are State-based.

Whilst we appreciate that there are some reforms to national transmission planning and the Regulatory Test in prospect following COAG's response to the ERIG recommendations, we have serious doubts that they will adequately address this problem.

3. Discussion Points

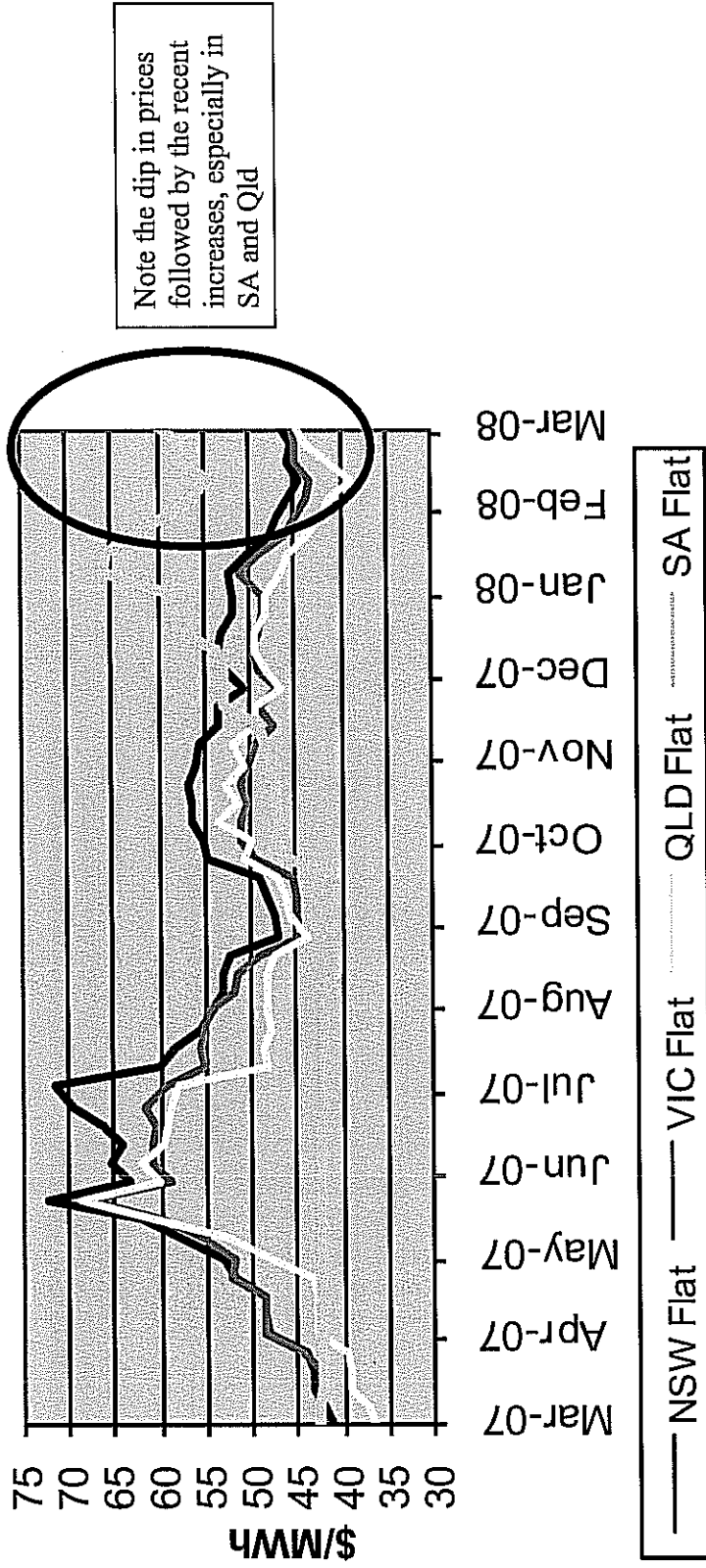
We believe this series of recent events highlights several potential market problems that we would wish to discuss with the AER/ACCC:

1. The process of market investigations undertaken by the AER, results so far and further work planned?

2. Whether any matters are arising that the AER is likely to seek further action on?
3. Whether any deficiencies in the market are becoming apparent through this work?
4. The efficacy of the bidding and re-bidding rules in the NEM, including the 'good faith' provisions and whether they can effectively discipline market power in circumstances such as those highlighted above?
5. The impact of the transmission constraints, whether these highlight deficiencies in inter-connector capacity and the ability of current arrangements such as the Regulatory Test to ensure optimal transmission capacity is available in the NEM? Whether the National Transmission Planner arrangement now being considered by MCE/AEMC is likely to lead to any concrete improvements?

ATTACHMENT A

2009 Flat Load Contact Price Path – As at 11 March 2008

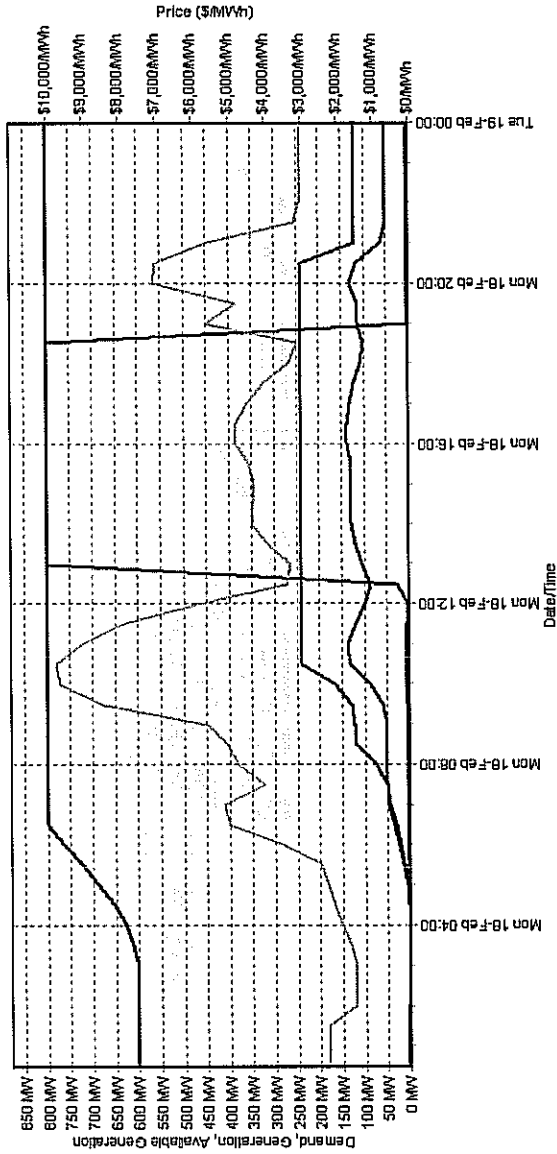


ATTACHMENT B

SA 18th February – Available and Actual Generation by AGL Torrens Island Plant

Market data between 18-02-2008 and 18-02-2008

Prepared on 7-03-2008



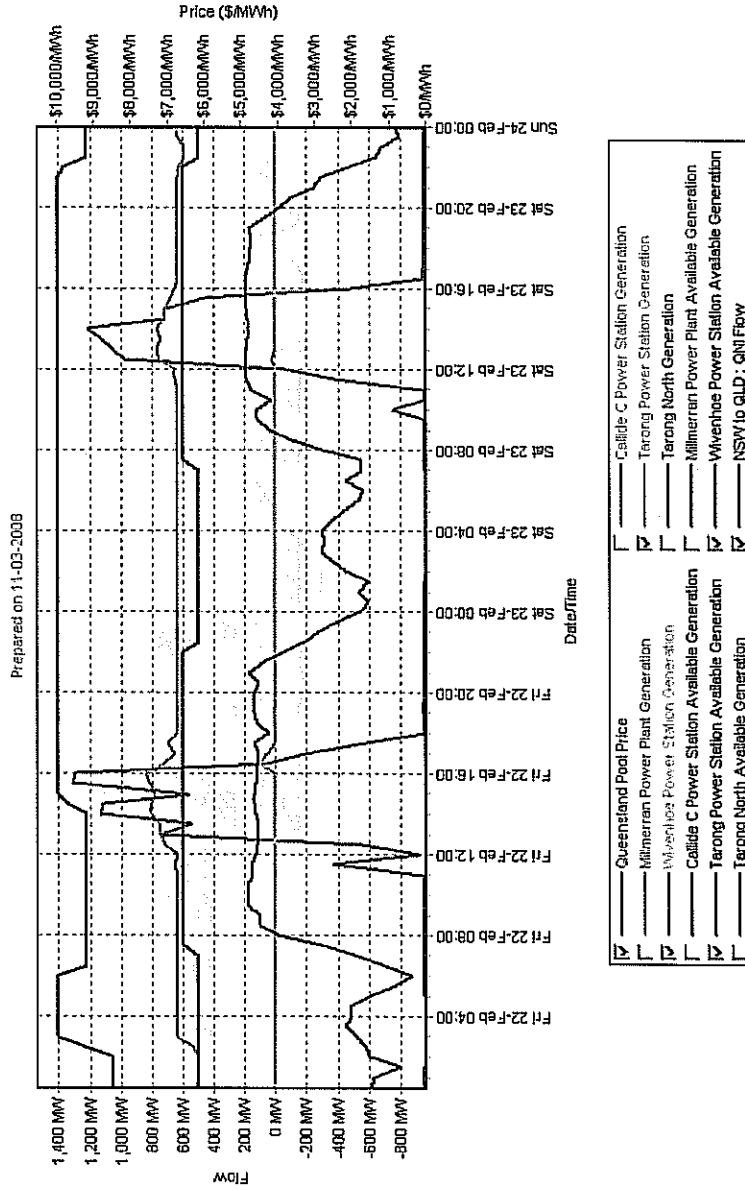
With reference to pool prices, this shows significant variation in generation to available levels for Torrens Island generation plant on 18 February. Similar generator offering was observed in the previous sustained price volatility event on 10 Jan.

<input checked="" type="checkbox"/>	South Australia Pool Price	<input checked="" type="checkbox"/>	Torrens Island Power Station A Generation
<input checked="" type="checkbox"/>	Torrens Island Power Station B Generation	<input checked="" type="checkbox"/>	Torrens Island Power Station A Available Generation
<input checked="" type="checkbox"/>	Torrens Island Power Station B Available Generation	<input type="checkbox"/>	Hallett Generation
<input type="checkbox"/>	Somerton Generation	<input type="checkbox"/>	Hallett Available Generation
<input type="checkbox"/>	Somerton Available Generation		

Analysis produced with NEM-Review
www.nem-review.info

QLD 22 & 23 February - Available and Actual Generation by Tarong Energy

Market data between 22-02-2008 and 23-02-2008



This shows the difference in actual generation to available levels for 22 and 23 February. There is a difference of up to 900 MW in generation declared available and actual generation from Tarong Power Station. Although 600 MW was available from Wivenhoe Power Station, the amount of actual generation was negligible.