



Independent Market Operator

**Final Market Rule Change
Report:**

**Reserve Capacity refund price
calculation**

Ref: RC_2009_18

Date: 18 September 2009

1. INTRODUCTION

On 7 May 2009, the Independent Market Operator (IMO) submitted a Rule Change Proposal regarding the amendment of clause 4.26.1 of the Wholesale Electricity Market Rules (Market Rules).

This proposal was processed using the Standard Rule Change Process, described in section 2.7 of the Market Rules.

The standard process adheres to the following timelines:

The key dates in processing this Rule Change Proposal are:



The IMO's final decision is to accept the Rule Change Proposal. The detailed reasons for the IMO's decision are set out in section 7 of this report.

In making its final decision on the Rule Change Proposal, the IMO has taken into account:

- the Wholesale Market Objectives;
- the practicality and cost of implementing the proposal;
- the views of the Market Advisory Committee (MAC); and
- the submissions received.

All documents related to this Rule Change Proposal can be found on the IMO website: http://www.imowa.com.au/RC_2009_18

2. THE RULE CHANGE PROPOSAL

2.1 Submission Details

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Date submitted:	5 May 2009
Urgency:	Standard Rule Change Process
Change Proposal title:	Reserve Capacity Refund price calculation
Market Rule(s) affected:	4.26.1

2.2 Summary Details of the Proposal

Clause 4.29.1(b)ii of the Market Rules states that, if no Reserve Capacity Auction was held, the Monthly Reserve Capacity Price equals $(0.85 * \text{Maximum Reserve Capacity Price} * \text{Excess Capacity Adjustment})/12$. The Excess Capacity Adjustment reflects the extent of any surplus Capacity Credits assigned by the IMO above the Reserve Capacity Requirement for the relevant Capacity Year.

Clause 4.26.1 of the Market Rules includes a Refund Table used to calculate the Capacity Cost Refunds, which apply in the event that a Market Participant holding Capacity Credits does not meet its Reserve Capacity Obligations. The price variable “Y” in the Refund Table is calculated in the same way as the Monthly Reserve Capacity Price, except that there is no Excess Capacity Adjustment. It is therefore inconsistent with the Monthly Reserve Capacity Price, even though it is intended to be a refund of monies received by the Market Participant as consideration for providing Reserve Capacity.

The proposal is to amend Clause 4.26.1 so that it uses the Monthly Reserve Capacity Price calculated according to Clause 4.29.1.

The detailed information on the proposal is contained in Appendix 1 and can be found in both the Rule Change Proposal and Draft Rule Change Report contained on the IMO’s website.

2.3 The Proposal and the Wholesale Market Objectives

In the Rule Change Proposal, the IMO submitted that it considers that the proposed Amending Rules remove ambiguity, provide consistency in the calculation of both payments to holders of Capacity Credits and any Capacity Cost Refund amounts, while recognising any oversupply of capacity as considered by the ECA concept. This improves the integrity of the Market Rules, and therefore is consistent with the operation of the Wholesale Market Objectives.

2.4 The Amending Rules Proposed by the IMO

The Amending Rules originally proposed by the IMO were presented in the Rule Change Notice, available on the IMO website.

2.5 The IMO's Initial Assessment of the Proposal

The IMO decided to proceed with the proposal on the basis of its preliminary assessment, which indicated that the proposal was consistent with the Wholesale Market Objectives.

3. FIRST SUBMISSION PERS

Griffin Energy considered that the Rule Change Proposal is an amendment to the Market Rules which does not seek to better facilitate specific objectives of the market, but one which maintains the ability of the Market Rules to function in a way that allows the Wholesale Market Objectives to be met.

Griffin Energy considered that the Rule Change Proposal appears consistent with all the Wholesale Market Objectives.

3.1.2 Submission from Landfill Gas and Power

LGP supported the Rule Change Proposal on the grounds that it corrects an unintended consequence of an earlier rule change.



LGP considered that this Rule Change Proposal is consistent with all objectives, as it maintains the integrity of the Market Rules.

3.1.4 Submission from Synergy

Synergy considered that consistency in capacity price and refund calculations should apply, but contended that there is a historically based reason for the inconsistency.

Synergy contended that there is a justifiable value difference related to the level of security between capacity costs and refunds when excess capa

In preparing its Final Rule Change Report, the IMO must assess the Rule Change Proposal in light of clauses 2.4.2 and 2.4.3 of the Market Rules.

Market Rule 2.4.2 outlines that the IMO “ *t nq*  *A n*  *n t t* ”

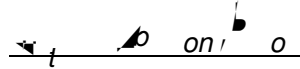
Cost Refund amounts, while recognising any oversupply of capacity as considered by the ECA concept. The IMO contends that this improves the integrity of the Market Rules, and therefore is consistent with the Wholesale Market Objectives.

7.2 Practicality and cost of implementation

The proposed changes do not require any change to the Wholesale Electricity Market Systems operated by the IMO.

There have been no additional costs identified with the implementation of this Rule Change Proposal.

7.3 Views expressed in submissions

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Four submissions were received during the first submission period. Three of these (Alinta, Griffin Energy and LGP) supported the proposed Amending Rules, the fourth (Sj7(u)-0.115971(l)1.4.98(f)-

- have the support of the MAC; and
- have the support of the majority of submissions received.

per MW shortfall per Trading Interval) Maximum Participant Refund				
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APPENDIX 1: FULL DETAILS OF THE PROPOSAL

Clause 4.26.1 of the Market Rules includes a Refund Table, which is used to calculate the Capacity Cost Refunds. This Refund Table is used to calculate the Capacity Cost Refunds that would be applied in the event that a Market Participant which holds Capacity Credits does not meet its Reserve Capacity Obligations. The price variable “Y” in the Refund Table is expressed as a dollar per megawatt (MW) per Trading Interval

$$\begin{aligned}
 \text{ECA} &= \frac{\text{RCR}}{\text{CC}} \\
 &= \frac{4322}{4599.875} \\
 &= 0.9396
 \end{aligned}$$

The Monthly Reserve Capacity Price is based on the Maximum Reserve Capacity Price (\$122,500 for 2008/09 cycle) and is used to set the unit price of Capacity Credits paid to holders of Capacity Credits. It is also used to set the price at which refunds of those payments are paid.

Alternative one

When calculated in accordance with the method implied by clause 4.26.1:

$$\begin{aligned}
 \text{Monthly RCP} &= \frac{(\text{Max RCP} * 0.85)}{12} \\
 &= \frac{(122,500 * 0.85)}{12} \\
 &= \$8677.08
 \end{aligned}$$

Alternative two

When calculated in accordance with the method given by 4.29.1, yields the following value:

$$\begin{aligned}
 \text{Monthly RCP} &= \frac{(\text{Max RCP} * 0.85 * \text{ECA})}{12} \\
 &= \frac{(122,500 * 0.85 * 0.9396)}{12} \\
 &= \$8152.91
 \end{aligned}$$

In the absence of clarity within the Market Rules, there are three options available for settlement purposes:

1. **Option one:** Apply alternative one (clause 4.26.1) to both Capacity Credit payments and Capacity Cost Refund calculations. This would have the effect not taking into account the ECA factor and, as a result, overcharging Market Customers for Reserve Capacity.
2. **Option two:** Apply alternative two (clause 4.29.1) to both Capacity Credit payments and Capacity Cost Refund calculations. This means that the definition in the table of MR

4.26.1 is not applied, but ensures payments for Capacity Credits and Capacity Cost Refund amounts are consistently applied by taking into account oversupply via the ECA.

3. **Option three:** Apply alternative one (clause 4.26.1) to Capacity Cost Refund calculations, and alternative two (clause 4.29.1) to Capacity Credit payments which would result in holders of Capacity Credits being charged more in relation to the payments with regards to Capacity Cost Refund amounts.

The IMO settlement applications are currently configured to apply option two (which is applying the interpretation in clause 4.29.1 to both Capacity Credit payments and Capacity Cost Refund calculations).

Original Proposal

The IMO contended that:

- clause 4.26.1 should have been amended to reflect the calculation methodology in 4.29.1 when changes were made to the Market Rules when the ECA concept was introduced (see Gazette No 143, 18th August 2006);
- option one, applying the calculation methodology in clause 4.26.1, would be inconsistent with the desired intent of providing a price response to uncontracted capacity in the market as introduced via the ECA provisions; and
- the intent of clause 4.26.1 is, and should be, to calculate the value Y on a Trading Interval basis, where Y equals the Monthly Reserve Capacity Price (calculated in accordance with clause 4.29.1) divided by the number of Trading Intervals in the relevant month. This value is then scaled in the Refund Table to take into account whether the failure to satisfy the Reserve Capacity Obligations occurred in a peak trading interval. Calculating Y in this manner would then explicitly incorporate the Excess Capacity Adjustment Value in the calculations of any Capacity Cost Refunds. Therefore the IMO recommends that the calculation methodology of 4.29.1 should be applied to both Capacity Credit payments and Capacity Cost Refund calculations.

The objective of this Rule Change Proposal is to provide clarity around the calculation of the Capacity Cost Refunds and to link the calculation of these refunds to the Monthly Reserve Capacity Price (as defined in 4.29.1), ensuring that both the original payment for Capacity