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Comments on Staff Paper on Power Market Pricing

Background: CERC has issued the staff paper in October 2022 on the matter on Power Market Pricing in view of the recent high prices discovered in the Power Exchanges. The Staff paper explored various aspects which led to high prices. The paper discussed the current Short Term market scenario, products of Power Exchanges, issues in pricing mechanism, global market design and developments, and proposed Pay as Bid mechanism. Comments are solicited on the matters covered in the paper.

After carefully analysing and deliberating the points raised in the Paper, we hereby submit our comments. The comments are given below.

- The prices discovered in Power Exchanges are function of demand and supply in Short- Term market. However, the demand in Short-Term is also linked with the Demand/Supply management under Long Term arrangements. If DISCOMs are not able to secure supply under Long Term arrangements, such demand is bound to shift to Short Term market, thus affecting the prices in Short Term Market. Hence, looking at Short-Term Market pricing mechanism in isolation is not appropriate. Hon'ble Commission must also look into the matter of availability of fuel especially the domestic coal and the actions of the PSUs and the generating companies owned by the States during the period under consideration.

  It is requested that Hon'ble Commission take a holistic view of Market design of over all market including Long Term Market and fuel market.

- In the second section 'Issues in Pricing Methodology', reference has been given to the 'extra profits' and 'Sellers surplus' and these points has been cited as reason which prompted the discussion on the different possible pricing methodologies.
  Here, we need to understand how 'Seller Surplus' increases. The 'Seller Surplus' increases when either the MCP increase or the seller's bid point decrease. In current situation, the increase in MCP led to increase of 'Seller Surplus'. Here it is important to understand the situation which led to increase in MCP. The MCP touched abnormally high price as few DISCOMs, who are primary market driver, started putting buy bids at Cap level. This led to MCP reaching to Rs20/kWh or Rs12/kWh even when sellers were putting sell bids at lower price. Thus the current 'High Seller Surplus' is making of the desperate behaviour of Buying entities. The buying behaviour of any DISCOM in Short Term is linked to it's over all power management strategy including Long Term arrangements.

  Hence it is requested that the real root cause analysis be done for the situation rather than raising unfounded concerns on high gains to the sellers.

- The staff paper, while elaborating on 'Seller's Surplus' completely ignored the concept of 'Buyer's surplus'. The proposed 'Pay-As-Bid' mechanism proposes that the Seller be paid as per their bid, thus the 'Seller's Surplus' would be captured by the Market operator. It is understood that the Hon'ble Commission would set a mechanism to transfer such surplus to eligible beneficiaries. However, the natural economic justice also calls for parity in terms of treatment given to the entities which participate in the market.

Hence it would be appropriate that the Pay-As-Bid be applicable on the Buyer Entities i.e. these entities should pay for the energy at their bid price rather than MCP; and there should be mechanism to capture such 'Buyer's Surplus' by the Market operator, which needs to be passed on to eligible beneficiaries along with 'Seller's Surplus'.

- We need to understand the difference between 'Spikes in Price' and 'Sustained higher prices' while dealing with the questions of Market Design and the Signals to stakeholders. The sustained higher prices give signals to the project developers to set up new generation capacities. Whereas the Spikes in prices for short duration lacks signalling power for creating New Capacities. But the spikes do signals to existing costlier generating assets to ramp up the generation. Now, basis the 'Spikes in Prices' if we start changing the market design, the market may end up losing the correct signalling power.

  Consider a situation in 'Pay-as-Bid' mechanism whereas sellers/generators are paid as per their bid (considering they bid at their marginal price) rather than MCP, the developers will not have any incentives to setup capacities for short term market. Further, they will opt for fixed long term PPAs where they are saved from uncertainties of getting despatches associated with power exchanges. This will result into less of power being made available in Short Term market.

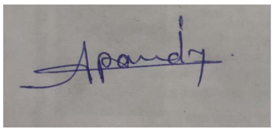
  We can also visualize a situation in 'Pay-As-Bid' mechanism where the Sellers/Generators will start putting their sell bid at a higher rate than their marginal price. This will push the MCP on the higher side. In effect there will be market distortion.

  Hence it is requested that the Hon'ble Commission consider the market signalling aspect before considering the 'Pay-As-Bid' mechanism.

- The staff paper rightly raised the points of Regulatory interventions and the basis of interventions. The suggestion of setting up of tolerance level is a welcome step. For that, Hon'ble commission may monitor the average prices on weekly basis and if there is upward movement of average MCP by 100% the commission should intervene by setting the lower cap price.
- The suggestion of clawback of profits made by the seller/generators goes against the principle of Signalling hence should not be considered.
- The point number 3.3.2 of staff paper discusses the scenario where high cost/marginal generator seems to be setting the market clearing price. However, we have seen that the MCP is set by the few buying DISCOMs hence the concern raised is unfounded.

- The staff paper also sought suggestion for market design for 'Demand response' and 'Energy Storage System'. Currently cost of ESS is high but it is expected that when ESS achieves the economy of scale, the cost will come down. Till then ESS needs to be incentivised/ supported so that these can compete with other source of power in the market. This could be done by creating capacity market for such assets. To support such capacity market, DISCOMs/Buyers should be mandated to secure some % of their demand through ESS. A robust compliance monitoring of such mechanism will go in long way in creating ESS capacities.

Regards,



Abhishek Pandey

For AMP Energy Markets Pvt Ltd