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Australian Energy Market Commission

## **DRAFT RULE DETERMINATION**

# NATIONAL ELECTRICITY AMENDMENT (EXTENSION OF THE APPLICATION OF THE IRM TO THE RRO) RULE

Australian Energy Market Operator

13 JULY 2023

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# DETERMINATION

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## ABOUT THE AEMC

The AEMC reports to the energy ministers. We have two functions. We make and amend the national electricity, gas and energy retail rules and conduct independent reviews for the energy ministers.

## ACKNOWLEDGEMENT OF COUNTRY

The AEMC acknowledges and shows respect for the traditional custodians of the many different lands across Australia on which we all live and work. We pay respect to all Elders past and present and the continuing connection of Aboriginal and Torres Strait Islander peoples to Country. The AEMC office is located on the land traditionally owned by the Gadigal people of the Eora nation.

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## CITATION

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## EXECUTIVE SUMMARY

- 1 The Australian Energy Market Commission (the AEMC or Commission) has decided to make a draft rule to extend the application of the interim reliability measure (IRM) to the retailer reliability obligation (RRO) to 30 June 2028. This is in response to a rule change request from the Australian Energy Market Operator (AEMO).
- 2 Given the size and pace of the energy market transition between now and 2028, the Commission considers that extending the IRM as a risk management tool is in the long-term interests of consumers.
- 3 The Commission intends to review whether further measures like the IRM are needed beyond 1 July 2028 following the 2026 Reliability Standards and Settings Review when a longer-term approach to managing reliability tail risk is known.<sup>1</sup> If necessary, the Commission will review the need for the IRM beyond 30 June 2028, following the Reliability Panel's (the Panel's) 2026 Reliability Standards and Settings Review.
- 4 The Commission has decided to fast-track this rule change request. This is because it concluded that the rule change request is consistent with the relevant recommendation of the AEMC's 2023 Review of the Interim Reliability Measure (2023 IRM Review) and adequate consultation with the public was carried out on the relevant recommendation.
- 5 We are seeking feedback on our draft determination and rule by **24 August 2023**.

### While stakeholders had mixed views, the Commission considers the draft rule is in the long-term interest of consumers

- 6 The Commission considers the draft rule to extend the application of the IRM to the RRO will contribute to the achievement of the national electricity objective (NEO).
- 7 In making its draft determination, the Commission considered the findings of the 2023 IRM Review and the feedback from stakeholders provided during the review. In particular, the Commission's findings that removing the IRM as the trigger for the RRO between 1 July 2025 and 30 June 2028 could increase uncertainty about the reliability framework and how tail risk is being managed as the power system transitions to a high VRE power system.
- 8 In response to the 2023 IRM review, the Commission received eight submissions from stakeholders on its draft recommendation to extend the application of the IRM to the RRO by three years. Of the eight, two supported the draft recommendation, five did not support and one was neutral on the need for the IRM.
- 9 Stakeholders made valid points that the RRO being triggered by the IRM may lead to increased costs as it may result in the RRO being triggered more often. The Commission has taken these points into account in response to AEMO's rule change request. In balancing the options, the Commission is of the view that, despite the risk of increased costs, the draft rule to extend the IRM is warranted in light of the changing nature of the drivers of reliability risk.

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<sup>1</sup> Tail risk represents low probability events that would have a high impact on reliability outcomes. For example, rare large-scale weather events which mean variable renewable energy resources (VRE) cannot generate to their full capacity.

- 10 The IRM plays an important role in addressing tail risk over the period 1 July 2025 to 30 June 2028 as the market transitions to a high VRE and energy-limited power system. The Commission considers that maintaining the IRM as a supplementary measure while the Panel reviews the form of the reliability standard provides greater certainty to the market on the reliability framework until July 2028.
- 11 Some stakeholders provided feedback that the Commission should have considered the Panel's recent decision on the level of the reliability standard. However, the Commission notes that the Panel has recommended that a standard of 0.002 per cent unserved energy (USE) reflects the value customers place on reliability for the purpose of the market settings. The Commission supports the Panel's process. However, it considers that the IRM is an additional measure to the market settings to protect customers from increasing reliability risks during the period before the Panel has completed its work on the form of the reliability standard.
- 12 The Panel has recognised the need to develop a standard that appropriately addresses tail risk and estimates that this risk may not eventuate until after 2028. The Commission considers that retaining the tighter interim standard until the new standard is in place serves as a 'safety net' if this risk does emerge sooner. Given the low likelihood that the IRM will trigger the RRO more often, and therefore lead to additional costs, the Commission considers that it is an appropriate balance of the potential risk and cost compared to removing the standard.

### The draft rule includes a transitional arrangement for AEMO to request a T-3 instrument

- 13 The Commission has considered any potential impacts on the RRO in recommending an extension to the IRM and determined that a draft transitional rule is required. This draft transitional rule is to allow AEMO additional time to request a T-3 instrument if the 2023 Electricity Statement of Opportunities identifies a reliability gap in any region commencing on 1 December 2026.

## HOW TO MAKE A SUBMISSION

### We encourage you to make a submission

Stakeholders can help shape the solution by participating in the rule change process. Engaging with stakeholders helps us understand the potential impacts of our decisions and contributes to well-informed, high-quality rule changes.

### How to make a written submission

**Due date:** Written submissions responding to this draft determination and rule must be lodged with Commission by **24 August 2023**.

**How to submit:** Go to the Commission's website, [www.aemc.gov.au](http://www.aemc.gov.au), find the "lodge a submission" function under the "Contact Us" tab, and select the project reference code ERC0366.<sup>2</sup> Tips for making submissions are available on our website.<sup>3</sup>

**Publication:** The Commission publishes submissions on its website. However, we will not publish parts of a submission that we agree are confidential or that we consider inappropriate (for example, offensive or defamatory content or content likely to infringe intellectual property rights).<sup>4</sup>

### Next steps and opportunities for engagement

There are other opportunities for you to engage with us, such as one-on-one discussions. Following consultation on this draft determination and rule, the Commission will publish a final determination and rule on 21 September 2023.

You can also request that the Commission hold a public hearing about this draft rule determination.<sup>5</sup>

**Due date:** Requests for a hearing must be lodged with the Commission by 20 July 2023.

**How to request a hearing:** Go to the Commission's website, [www.aemc.gov.au](http://www.aemc.gov.au), find the "lodge a submission" function under the "Contact Us" tab, and select the project reference code **ERC0366**. Specify in the comment field that you are requesting a hearing rather than submitting.<sup>6</sup>

Please contact the project leader with questions or feedback at any stage.

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2 If you are not able to lodge a submission online, please contact us, and we will provide instructions for alternative methods to lodge the submission.

3 See: <https://www.aemc.gov.au/our-work/changing-energy-rules-unique-process/making-rule-change-request/our-work-3>

4 Further information about the publication of submissions and our privacy policy can be found here: <https://www.aemc.gov.au/contact-us/lodge-submission>

5 Section 101(1a) of the NEL.

6 If you cannot lodge a request online, please contact us, and we will provide instructions for alternative methods.

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# 1 THE COMMISSION HAS MADE A DRAFT DETERMINATION

The Australian Energy Market Commission's (the AEMC or Commission) draft determination is to make a draft electricity rule in response to a rule change request submitted by the Australian Energy Market Operator (AEMO) to extend the application of the interim reliability measure (IRM) to the retailer reliability obligation (RRO).

The Commission's reasons for making the draft determination are set out in chapter 2. Information on the legal requirements for making the determination is found in appendix D.

## 1.1 Our draft rule extends the application of the IRM to the RRO by three years

The Commission's draft rule extends the IRM as it applies to the RRO to 30 June 2028.<sup>7</sup>

The national electricity market (NEM) is undergoing a significant transformation. It is shifting from a capacity-limited thermal power system to a more energy-limited power system characterised by high levels of variable renewable energy (VRE). The transformation requires careful consideration of how reliability is characterised and managed to ensure the system can meet customer demand at a level they value. In light of this, the Reliability Panel (the Panel) is reviewing the need for a new form of the reliability standard, and while this is underway, continuing the IRM is a mechanism to address tail risk in the reliability framework.

The Commission is satisfied that the final recommendation of the Review of the IRM (2023 IRM Review) aligns with other aspects of the broader NEM reliability framework and is likely to better contribute to the achievement of the national electricity objective (NEO) while the Panel does further work on understanding tail risk.

## 1.2 Stakeholders had mixed views on the IRM Review recommendations

Through the IRM Review, stakeholders provided feedback on the IRM. This section summarises the feedback we received and how it shaped the draft determination.

Of the eight submissions received through the 2023 IRM Review, two supported the recommendation, five did not support, and one was neutral on the need for the IRM. The Commission is satisfied that the recommendation to extend the IRM's application to the RRO by three years was consulted on and meets the criteria for a fast-track rule change.

Stakeholders made valid points that the RRO being triggered by the IRM may lead to increased costs as it may result in the RRO being triggered more often. The Commission has taken these points into account in balancing the options and considers that, despite the risk of increased costs, the draft rule to extend the IRM is warranted in light of the changing drivers of reliability risk in the power system.

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<sup>7</sup> Clauses 4A.A.2 and 11.132.2 of the NER.

### 1.2.1 **There were mixed views on whether the IRM is needed to address reliability risk**

AEMO and Hydro Tasmania noted that the IRM plays an interim role in addressing tail risk until a new form of the reliability standard is in place. Hydro Tasmania argued, “[a]t a time when the NEM is rapidly evolving and reliability outcomes are less certain than historically, Hydro Tasmania understands and appreciates the rationale for extending the application of the IRM for a period of three years”.<sup>8</sup>

AEMO noted that “the IRM continues to be an appropriate interim risk management tool and an important temporary measure to support the changing nature of reliability risk. The 0.0006% unserved energy (USE) standard continues to supplement the reliability standard to meet consumer expectations per its original design”.<sup>9</sup>

The Australian Energy Council (AEC), Alinta Energy, Energy Australia, Energy Users Association of Australia (EUAA) and Shell Energy considered that the existing market settings and mechanisms based on the reliability standard should play the primary role of addressing tail risk, reflecting the value that consumers place on reliability.<sup>10</sup> Energy Australia further noted that potential new measures like the Commonwealth’s Capacity Investment Scheme could further support reliability which addresses tail risk.<sup>11</sup> The Reliability Panel recognised the need to develop a standard that appropriately addresses ‘tail risk’ and estimates that this risk may not eventuate until after 2028.

### 1.2.2 **Some submissions consider an extension would create an inconsistent framework**

Some stakeholders noted that the use of the IRM, conflicted with the reliability standard of 0.002 per cent and that the IRM creates uncertainty in the market. Alinta Energy argued, “the IRM also adds complexity to the market, by introducing [a] competing and inconsistent standard with the reliability standard”.<sup>12</sup> The AEC considered that the Reliability Panel should be the body responsible for setting reliability standards.<sup>13</sup> However, AEMO “considers that the continued use of the IRM as the trigger for the RRO appropriately signals an upcoming need for investment in firm generation at the level that aligns with community expectations of reliable electricity supply during a one-in-10-year summer, at lowest cost to the market”.<sup>14</sup>

The Commission considers that extending the IRM is a consistent NEM-wide approach to managing reliability risk embedded in the NEL and NER and is preferable to different jurisdictional approaches. The work by the Panel on the form of the standard, along with the 2026 review of the reliability standards and settings, will be critical to establishing a NEM-wide approach to addressing tail risk from 1 July 2028.

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8 Hydro Tasmania, (April 2023) Submission to the 2023 IRM Review: 1.

9 AEMO, (April 2023) Submission to the 2023 IRM Review: 2.

10 Submissions to the 2023 IRM Review: AEC pg, 1, Alinta pg 2-3, Energy Australia pg 1, EUAA pg 2 and Shell Energy pg 2.

11 Energy Australia, (April 2023) Submission to the IRM Review: 3.

12 Alinta Energy, (April 2023) Submission to the 2023 IRM Review: 3.

13 AEC, (April 2023) Submission to the 2023 IRM Review.

14 AEMO, (April 2023) Submission to the 2023 IRM Review: 3.



### 1.2.3 **Five review submissions indicated that the IRM results in higher costs**

The Commission recognises that there were different views in submissions on the potential costs of an extension.

Submissions from the AEC, Alinta Energy, EUAA, Energy Australia and Shell Energy considered that extending the IRM will potentially deliver higher costs to consumers, as it may be triggered more often and will result in an increased regulatory burden to liable entities. In AEMO's view, however, the costs on liable entities would be limited as they are only required to contract to cover their share of one-in-two-year peak demand rather than contracting to the 0.006 per cent USE standard.

## 1.3 **Extending the IRM supports certainty in the reliability framework**

Energy Ministers established the IRM as a temporary measure to protect customers from increasing reliability risks, particularly low-probability events that could have a high impact on reliability outcomes, while a longer-term market design is developed.

The IRM supports reliability by supplementing the existing reliability standards by triggering RRO requirements that liable entities must enter into sufficient qualifying contracts to meet their share of expected system peak electricity demand on a 50 per cent probability of exceedance (PoE) (one-in-two year demand peak).

Since the IRM was introduced, the Panel has recommended maintaining the reliability standard at 0.002 per cent USE. In the Panel's view, 0.002 per cent meets the value customers place on reliability for the purposes of market settings.<sup>15</sup> The Panel also recommended reviewing a new form of the reliability standard to more comprehensively address tail risk. Any new form of reliability standard the Panel may recommend is expected to be in place by 1 July 2028.

The Commission did not repeat the Panel's work in the review of the IRM or for this rule change. However, the Commission acknowledges the Panel's recommendation that reliability risk, particularly tail risk, may need to be characterised differently as the market transitions to net zero by 2050. The Commission considers that maintaining the IRM as a supplementary measure while the Panel reviews the form of the reliability standard provides greater certainty to the market to 1 July 2028. Further, given the size and pace of the energy market transition between now and 2028, the Commission does not consider it is in the interest of consumers to remove the IRM as a risk management tool before the Panel has considered the reliability standard.

Once decisions on the form of the reliability standard are known and following the 2026 Reliability Standards and Settings Review, the Commission intends to review whether further measures like the IRM are needed beyond 1 July 2028.

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<sup>15</sup> The reliability standard is a key input for market price settings which include the Market Price Cap (MPC) and Cumulative Price Threshold (CPT). The market price settings provide financial incentives to market participants for operational decisions and to invest in energy infrastructure, supporting reliability in the NEM.

## 1.4 Keeping the IRM provides a market-wide solution to reliability

Extending the IRM as the trigger for the RRO to 30 June 2028 aligns with the decision by Ministers to extend the Interim Reliability Reserve (IRR) to 2028 and creates a consistent approach on the use of the IRM until that time.<sup>16</sup> Further, given the Panel's work to determine the long-term reliability framework, the Commission considers an extension of the IRM would minimise the administrative impact of changing the standard several times over a short period.

Further, the Commission notes the stakeholder feedback that the market has been assuming that the IRM would expire on 30 June 2025, and therefore we would be creating more uncertainty by extending it. When Ministers introduced the IRM, it was intended to be in place until such time as a more enduring market design was implemented. To that end, Ministers included a review requirement in the rules rather than a specific end date. Under section 45 of the NEL, the AEMC may conduct reviews into the operation and effectiveness of the Rules as it considers appropriate. The Commission may decide to review the IRM closer to the extended 2028 date (if necessary).

## 1.5 The risk of additional costs associated with an extension are low

The Commission has considered potential impacts on consumers in light of current energy cost increases. There have been recent changes to the RRO and IRR which mean the main cost impact on consumers of extending the IRM is limited to its use as a trigger for the RRO:

- a recent rule change enables contracting under the IRR to be extended to 2028
- a change to the NEL allows Ministers in participating jurisdictions to make a T-3 instrument.<sup>17</sup>

The Commission considers the incremental costs of the extension of the IRM are likely to be low if it only triggers T-3 obligations. T-3 reliability gap costs are limited to reporting costs and any market making actions. These costs are expected to be low in the context of broader system costs. T-1 RRO costs (if they are realised) are potentially higher, comprising Procurer of Last Resort (PoLR) costs, contracting costs and potentially penalties for non-compliance:

- For customers of non-compliant liable entities, these costs may be significant, but with the purpose of reducing instances of unserved energy which can in themselves place a significant cost burden on the broader community.
- Liable entities have three years notice at T-3 about the need to comply with the RRO and therefore contract to sufficient levels to protect their customers from these costs. While there will be higher contracting costs at T-1 for liable entities required to contract to a one in two year peak demand, these costs are not likely to be significant if entities enter contracts early.

<sup>16</sup> The IRR is an out-of-market capacity reserve that allows AEMO to enter multi-year reserve contracts for reliability.

<sup>17</sup> the National Electricity (South Australia) (Ministerial Reliability Instrument) Amendment Act 2023 (No 8 of 2023) came into operation on 14 April 2023 and allows Ministers to make a T-3 instrument if it appears to the Minister on reasonable grounds that there is a real risk during a period specified in the instrument (NEL s14JA (1)).

Some stakeholders provided feedback to the 2023 IRM review that the Commission had not considered the Panel's recent decision on the level of the reliability standard. They stated that the Panel has recommended a standard that reflected the level of reliability customers value and the IRM is above that level. However, the Commission notes that the IRM has limited application, compared to the reliability standard.

The reliability standard is a key input for the market price cap (MPC) and cumulative price threshold (CPT). The MPC and CPT are the critical investment signals for the NEM. They are set at levels that are sufficiently high to support the investment required to achieve reliability outcomes consistent with the standard, but not too high to create systemic financial risks that may compromise the stability of the market.<sup>18</sup> The IRM itself is not used to set the level of the MPC. It is an additional risk management tool that may contribute to reliability by triggering requirements on retailers to contract for their load and to enable AEMO to contract for out of market reserves.

Further information on the Commission's views on the risk of additional costs is provided in appendix B.

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<sup>18</sup> Reliability Panel, *2022 Review of the Reliability Standard and Settings, Final Report*, p. 63.

## 2 EXTENDING THE IRM CONTRIBUTES TO THE NEO

The Commission can only make a rule if it is satisfied it will or is likely to contribute to the achievement of the relevant energy objective.<sup>19</sup>

For this rule change, the relevant energy objective is the NEO:

to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to:

1. price, quality, safety, reliability and security of supply of electricity; and
2. the reliability, safety and security of the national electricity system.

The draft rule is likely to better contribute to the achievement of the NEO by providing predictability, transparency, and stability for the market while the Panel does further work on understanding 'tail risk.'

In developing the draft rule, the Commission has considered the application to the Northern Territory according to the following questions:

- Should the NEO test include the Northern Territory electricity systems? Yes, for this rule change request the Commission proposes to determine that the reference to the "national electricity system" in the NEO includes the local electricity systems in the Northern Territory, as well as the national electricity system.
- Should the rule be different in the Northern Territory? No, the draft rule determination is to make a uniform rule because the different physical characteristics of the Northern Territory's network would not affect the operation of the draft rule in such a way that a differential rule would better achieve the NEO in this instance.

See appendix D for more detail on the legal requirements for a decision.

### 2.1 Extending the IRM is the best course of action when assessed against our criteria

The Commission has considered the NEO<sup>20</sup> and the issues raised in the rule change request and have assessed the draft rule against five assessment criteria outlined below.

1. **Safety, security, reliability and principles of market efficiency:** the regulatory framework should contribute to reliability outcomes in the NEM and promote efficiency across investment/planning, commitment and dispatch timeframes.
2. **Appropriate allocation of risk:** Risks should be borne by parties who are in the best position to manage them and have the incentives to do so.
3. **Timing and practicality:** Any proposed changes should consider how likely a practical policy solution will be developed and implemented. Additionally, changes should achieve the intended benefits in a timely, proportionate, and targeted way.

<sup>19</sup> Section 88(1) of the NEL.

<sup>20</sup> Section 7 of the NEL.

4. **Predictability and stability:** The regulatory framework should promote confidence in the market by clearly defining roles and responsibilities and ensuring that parties have sufficient information to make decisions. The framework should also result in predictable outcomes for all participants.
5. **Simplicity and transparency:** The regulatory framework should be as simple and practicable as possible and provide parties with sufficient information to make decisions.
6. **Success as a market-wide solution and consideration of the broader direction of reform:** Changes should align with the Reliability Panel's review to promote a market-wide solution and deliver a consistent reliability framework across the NEM.

We gathered stakeholder feedback as part of the 2023 IRM Review and carried out a regulatory impact analysis in relation to these criteria.

The rest of this section explains why the draft rule best achieves the NEO when compared to other options and assessed against our criteria.

#### **2.1.1 The rule will be an effective tool in supporting a safe, secure and reliable system**

In initially recommending the IRM, the ESB considered that it is an appropriate interim risk management tool to meet community expectations that electricity supply remains reliable during a 1 in 10-year summer. The Commission considers that the IRM continues to meet this objective, pending the outcomes of the Panel's review of the new form of the reliability standard establishing an enduring approach to better manage tail risk from 1 July 2028.

#### **2.1.2 Risks created by the rule change will be borne by those in the best position to manage them**

Potentially higher risk of costs associated with the draft recommendation are only expected if a future ESOO forecast triggers T-1 reliability gaps above 0.0006 per cent USE and below 0.002 per cent between 2025-26 and 2027-28. The Commission notes that in the context of AEMO's 2022 ESOO and Update to the ESOO, the risk of T-1 costs would be low if 'expected and anticipated' projects become 'committed' projects over the three-year period.

Further, in April 2023, AEMO has updated its 2023 ESOO and Reliability Forecast Methodology Document such that the ESOO Reliability Forecasts (for the T-3 timeframe only) now include all production units that are existing, committed or anticipated.

#### **2.1.3 The timing of this rule change will work with other market activities and is a practical solution**

The draft rule requires only minimal changes to the NER, as the IRM is already implemented and operating. Reviewing the need for the IRM at a later date, and after the 2026 Reliability Standards and Settings Review allows for more data to be gathered on the effectiveness and need for the IRM, taking into account decisions on the new form of the reliability standard.

The release of the final rule determination on the interim measure will provide sufficient time for the market to respond to any reliability gaps identified in the ESOO.

**2.1.4 Providing predictability and stability while aligning with the broader direction of reform**

The final recommendation to extend the IRM, aligns with the decision by Ministers to extend the use of the IRM as it applies to the IRR to 2028. Extending the IRM as it applies to the RRO, therefore, maintains consistency in the approach to the IRM as a reliability measure in the NEM through to 30 June 2028, after which time the Panel's work on a new form of the reliability standard will establish an enduring approach to better-managing tail risk.

**2.1.5 The IRM is well understood, so will provide simplicity and transparency for market participants**

The IRM and its application to the RRO and IRR are already understood by industry and governments. Extending the IRM allows the market to operate in a simple and transparent manner while work is completed by the Panel on a new form of the reliability standard.

**2.1.6 Success as a market-wide solution and consideration of the broader direction of reform**

The draft rule will align with the Reliability Panel's review to promote a market-wide solution and deliver a consistent reliability framework across the NEM. This will ensure a stable and well-established tool is available to AEMO and the market to mitigate reliability risk.

## 3 HOW OUR RULE WOULD OPERATE

This draft rule will operate in the same way as the existing IRM for the purposes of the RRO which is currently set to expire on 30 June 2025. The rule is proposed to take effect on 21 September 2023.

The AEMC has considered the timing of this rule change and notes the importance of avoiding impacts on the operation of the RRO in its implementation. As such, in recommending an extension to the IRM, the Commission has determined that a draft transitional rule is required. This draft transitional rule ensures that in the event of the 2023 ESOO identifying a reliability gap in any region commencing on 1 December 2026, AEMO will have sufficient time to request a T-3 reliability instrument. Information on the draft transitional rule is outlined below.

### 3.1 The RRO timeline is based on AEMO releasing the ESOO by 31 August 2023

The RRO requires liable entities to hold contracts for their share of system peak demand when there is a forecast reliability gap. The current key steps for a T-3 instrument are set out below:

1. AEMO releases its ESOO by 31 August each year and identifies reliability gaps against the IRM or the reliability standard (NER clause 3.13.3A(a)(10)).
2. AEMO must apply to the AER for a T-3 instrument at least **three months** before the T-3 cut-off day (NER clause 4A.C.2(a)).
  - a. The T-3 cut-off day is the day that is three years before the start of the forecast reliability gap that AEMO identifies in the ESOO (NEL section 14G(3)).
  - b. This means that AEMO must apply to the AER at least **three years and three months** before T (T being the start of the reliability gap).
3. AEMO must only make the request if the reliability forecast published in the **6 months immediately preceding** the T-3 cut-off day identifies that forecast reliability gap (NER clause 4A.C.2(b)(3)).
4. The AER must within **two months** of receiving AEMO's request decide whether to make or not make the reliability instrument (NER clause 4A.C.9(c)).
5. The AER must publish its decision whether to make a reliability instrument on its website **before the T-3 cut-off day** or an earlier day prescribed by the Rules (NEL section 14K(6)).
6. The reliability instrument takes effect when it is published on the AER's website (NEL section 14K(5)).

### 3.2 The draft rule will not commence until 21 September 2023

The timing for this rule change request using the fast-tracked process means that the Commission cannot make a final determination before 21 September 2023, after which time AEMO will have released its 2023 ES00.

AEMO’s 2022 ES00 indicates a potential reliability gap in NSW against the IRM from 1 December 2026 – 28 February 2027. To ensure a T-3 reliability instrument can be in place for this period, AEMO would need to submit a request to the AER no later than 1 September 2023. However, AEMO will not be able to do this until such time as the Commission has made a final rule to extend the IRM beyond 30 June 2025. Figure 3.1 shows the current timeline.

**Figure 3.1: Timeline under current rules**



Source: AEMC

### 3.3 The Commission is making a draft transitional rule to give AEMO additional time

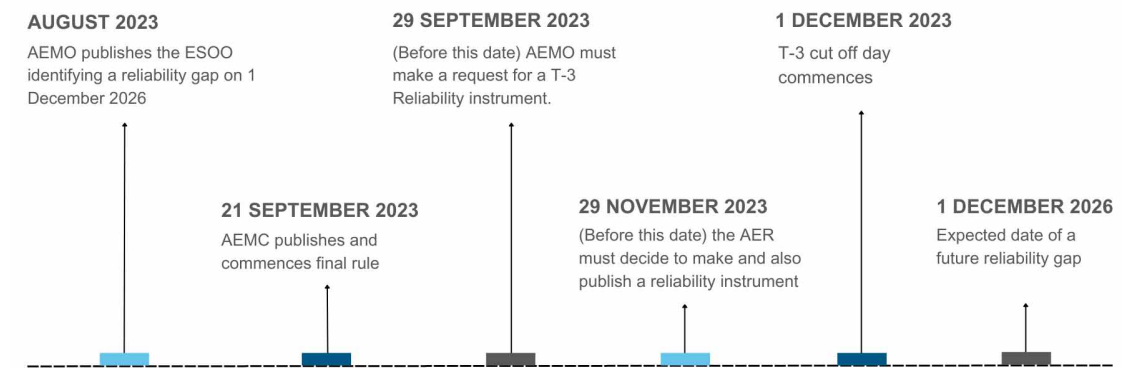
To address any difference in timing, we have proposed a draft transitional rule which will allow AEMO to apply for a T-3 instrument following the publication of the final rule. The draft transitional rule requires that if AEMO makes a request for a T-3 reliability instrument on or after 21 September 2023 and before 29 September 2023 it can make the request at least two months before the T-3 cut-off day for the relevant forecast reliability gap (rather than three months).

This ensures that if AEMO identifies a reliability gap for a region that starts on 1 December 2026 in the 2023 ES00 against the IRM, it will meet the statutory requirements in the NEL regarding the T-3 cut off day. The AER will still have two months to seek stakeholder feedback in accordance with the Reliability Instrument Guidelines and assess AEMO’s request against the relevant criteria. No other timelines in the RRO process will be affected. AEMO supports this approach.



Figure 3.2 summarises the updated timeline that would occur under the transitional rule if AEMO identifies any reliability gaps in a region from 1 December 2026.

**Figure 3.2: Proposed timeline under the draft transitional rule**



Source: AEMC

## A APPENDIX A — RULE MAKING PROCESS

A fast track rule change request includes the following stages:

- a proponent submits a rule change request
- the Commission commences the rule change process
- the Commission publishes a draft determination and draft rule (if relevant)
  - stakeholders lodge submissions on the draft determination and engage through other channels to make their views known to the AEMC project team
- the Commission publishes a final determination and final rule (if relevant).

You can find more information on the rule change process in *The Rule change process – a guide for stakeholders*.<sup>21</sup>

### A.1 AEMO proposed a rule to extend the operation of the IRM

AEMO has submitted a rule change to give effect to the Commission’s recent recommendation to extend the application of the IRM to the RRO to 30 June 2028.

The proposal seeks to address reliability risk, particularly tail risk, and increasing uncertainty as the power system transitions to zero-emissions generation by making available the IRM as a risk management tool.

### A.2 The process to date

On 13 July 2023, the Commission published a notice advising of its intention to initiate the rule making process in respect of the rule change request.<sup>22</sup> The Commission decided to fast-track this rule change request. This is because it concluded that the rule change request is consistent with the relevant recommendation of the Review into the Interim Reliability Measure and adequate consultation with the public was undertaken during that review on the relevant recommendation.<sup>23</sup>

Accordingly, the Commission did not publish a consultation paper upon initiation of the rule change process and there has been no formal consultation carried out in this rule change to date.

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21 AEMC, *The rule change process: a guide for stakeholders*, June 2017, available here: <https://www.aemc.gov.au/sites/default/files/2018-09/A-guide-to-the-rule-change-process-200617.PDF>

22 This notice was published under s. 95 of the NEL.

23 The decision to fast-track the rule change request was made under s. 96A(1) of the NEL.

## B RISKS OF ADDITIONAL COST ASSOCIATED WITH AN EXTENSION

### B.1 Extending the IRM trigger could result in the RRO applying more often

There are different costs incurred when the RRO is triggered at T-3 and T-1.

- T-3 RRO costs are limited to reporting costs and any market making actions. These costs are expected to be low in the context of broader system costs. The Regulatory Impact Statement (RIS) for the RRO estimated total business compliance costs across the NEM of \$77 million (or \$7.7 million per annum) over 10 years for the RRO.<sup>24</sup>
- T-1 RRO costs (if they are realised) are potentially higher, comprising Procurer of Last Resort (PoLR) costs, contracting costs and potentially penalties for non-compliance. For customers of non-compliant liable entities, these costs may be significant, but with the purpose of reducing instances of unserved energy which can in themselves place a significant cost burden on the broader community.

The IRM trigger may result in the RRO applying more often. As noted above, the main cost impact on customers of a liable entity of extending the IRM would be if a T-1 RRO is triggered more often by extending the IRM by three years to 2027-28.

The Commission considers the incremental costs of the extension of the IRM are likely to be low if it only triggers T-3 obligations. T-3 reliability gap costs are limited and do not place significantly higher costs on consumers.

Potentially higher costs through contracting and the PoLR cost recovery mechanism are largely incurred through RRO compliance with T-1 reliability gaps, which would only be realised if a gap continued to be in place one year (T-1) from the period of the gap (T). However liable entities have three years notice at T-3 about the need to comply with the RRO and therefore contract to sufficient levels to protect their customers from these costs. While there will be higher contracting costs at T-1 for liable entities required to contract to a one in two year peak demand, these costs are not likely to be significant if entities enter contracts early.

More significant costs can eventuate (at T) if system peak electricity demand is higher than a 50 per cent PoE and liable entities have not sufficiently contracted. These more significant costs are only born by the customers of individual liable entities which have not complied with the RRO by entering into sufficient qualifying contracts to meet their share of a 50 per cent PoE.

The Commission also notes the comments from stakeholders regarding the increase in contracting costs resulting from the IRM triggering a T-1 instrument. Contracting is key to the operation of the RRO, to encourage market investment and support reliability by reducing instances of USE that place a significant cost burden on the broader community. Conclusively identifying the cause of the increase in contracting costs from the RRO is difficult but the

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<sup>24</sup> Energy Security Board, *Retailer Reliability Obligation Decision Regulation Impact Statement* — 19 December 2018.

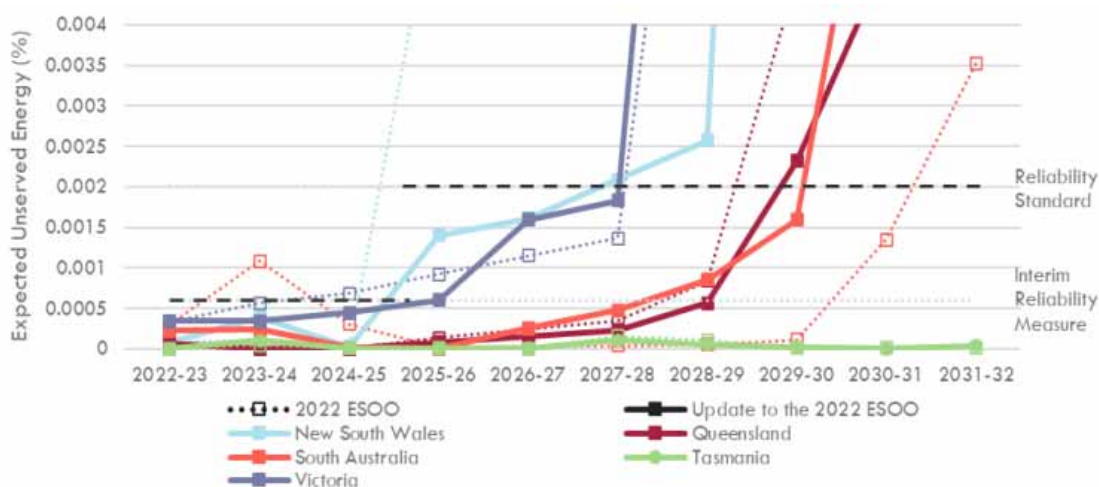
Commission agrees that contract costs appear to have risen in SA before the T-1 RRO contract position day. The Market Liquidity Obligation (MLO), which operated until the SA T-1, provided liable entities with the opportunity to purchase lower priced contracts to fulfil their forecast 50 per cent PoE customer demand by T-1.

## B.2 The risk of additional T-3 and T-1 trigger events is likely to be low

The Commission considers the incremental costs of the extension of the IRM would likely be low if it only triggers T-3 RRO requirements between 2025-26 and 2027-28 which do not translate into T-1 RRO requirements. The Commission notes that USE forecasts may be subject to change and that this may change its underlying assessment of costs.

Figure B.1 from AEMO’s Update to the 2022 Electricity Statement of Opportunities (ESOO) identifies reliability gaps in New South Wales (NSW) and Victoria over the period 2025-26 to 2027-28, which sit between 0.0006 per cent unserved energy (USE) and the Panel’s recommended reliability standard of 0.002 per cent USE.

**Figure B.1:** Reliability and indicative reliability forecast, all regions, 2022-23 to 2031-32



Source: AEMO, *Update to the Electricity Statement of Opportunities*, February 2023, p. 3

The Commission notes that in the *2022 ES00* and *Update to the 2022 ES00*, AEMO also assessed that if sufficient ‘anticipated and expected projects’ proceed as planned, this will potentially reduce reliability gaps below the IRM through to 2028-29. If these projects became ‘committed projects’, T-1 reliability gaps would not eventuate in future ES00 publications.

The *2022 ES00* notes that:<sup>25</sup>

An additional 3.4GW of ‘anticipated’ investments are in the pipeline and will improve the outlook if they progress as planned. When generation and storage projects classed

<sup>25</sup> AEMO 2022 Electricity Statement of Opportunities, pg 9.

as anticipated in the (2022) ESOO is considered alongside the anticipated and actionable transmission developments identified in the 2022 ISP, based on current schedules the reliability forecasts improves significantly. It shows that anticipated generation projects reduce forecast USE to below IRM and within the reliability standard' over coming years, until actionable transmission developments further support the reliability of these regions.

The *Update to the 2022 ESOO* notes that:<sup>26</sup>

While not yet sufficiently developed to meet AEMO's commitment criteria, many generation, storage and transmission developments are progressing, and if developed to their current anticipated schedules will lessen the reliability risk and reduce the forecast capacity requirements.

In addition, in April 2023 AEMO updated its ESOO and Reliability Forecast Methodology Document, such that the ESOO Reliability Forecast (for the T-3 timeframe only) now includes all production units that are existing, committed or anticipated in the most recent generation information page published in accordance with clause 3.7F of the NER.<sup>27</sup> Previously, anticipated projects were excluded from the ESOO Reliability Forecast. AEMO notes that the updated methodology seeks to include in the forecast "a greater number of projects that are likely to proceed, while sufficiently delaying developments that are less advanced and more prone to delays". By considering a broader range of production units that are likely to proceed to commissioning, AEMO may be less likely to determine a material reliability gap for the T-3 timeframe, other things being equal.

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<sup>26</sup> AEMO 2022 Update to the Electricity Statement of Opportunities, pg 5.

<sup>27</sup> AEMO, 2023 ESOO and Reliability Forecast Methodology Document.

## C REGULATORY IMPACT ANALYSIS

The Commission completed regulatory impact analysis to make its draft determination and has noted the following regarding impacts:

- The final recommendation to extend the IRM, aligns with the decision by Ministers to extend the use of the IRM as it applies to the IRR to 2028. Extending the IRM as it applies to the RRO, therefore, maintains consistency in the approach to the IRM as a reliability measure in the NEM through to 30 June 2028, after which time the Panel's work on a new form of the reliability standard will establish an enduring approach to better-managing tail risk.
- Costs could potentially be higher as the result of extending the IRM could mean the RRO is triggered more often. However, the Commission has already determined that despite the risk of increased costs, an extension to the IRM is warranted in light of the changing nature of the drivers of reliability risk.
- Only eight stakeholders provided submissions to the review of the IRM, five of which opposed the extension. We, therefore, anticipated limited new information to be provided by stakeholders as part of this rule change.

At this stage, our Regulatory Impact Plan is informed by the outcomes of the 2023 IRM Review. This review did extensive analysis of the regulatory impact and, as such, the AEMC expects that the impact of this rule change is likely to be the same as outlined in the review.

We note, however, that feedback received from stakeholders as part of the consultation on this draft rule change may reveal further regulatory impacts that were not previously considered. In this event, a regulatory impact analysis plan may be required. Further consideration of regulatory impacts will be considered following receipt of stakeholder submissions.

## D LEGAL REQUIREMENTS TO MAKE A RULE

This appendix sets out the relevant legal requirements under the NEL for the Commission to make a draft rule determination.

### D.1 Draft rule determination and draft rule

In accordance with section 99 of the NEL, the Commission has made this draft rule determination in relation to the rule proposed by AEMO.

The Commission's reasons for making this draft rule determination are set out in chapter 2.

A copy of the draft rule is attached to and published with this draft determination. Its key features are described in chapter 1 and chapter 3.

### D.2 Power to make the rule

The Commission is satisfied that the draft rule falls within the subject matter about which the Commission may make rules.

The draft rule falls within s. 34 of the NEL as it relates to:

- the operation of the national electricity system for the purposes of the safety, security and reliability of that system; and
- any matter or thing related to, or necessary or expedient for, the purposes of the RRO.

The draft rule also falls within the matters set out in Schedule 1 to the NEL as it relates to:

- the forecasting by AEMO for the purpose of the reliability obligation, and the process for AEMO to request a reliability instrument and the AER to make a reliability instrument (items 6A-6C); and
- reviews by the AEMC (item 33).

### D.3 Commission's considerations

In assessing the rule change request the Commission considered:

- its powers under the NEL to make the draft rule
- the rule change request
- submissions received during consultation as part of the 2023 IRM Review
- the Commission's analysis as to the ways in which the draft rule will or is likely to contribute to the achievement of the NEO.
- the application of the draft rule to the Northern Territory
- the timing of the release of the 2023 Electricity Statement of Opportunities (ESOO) by AEMO.

There is no relevant Ministerial Council on Energy (MCE) statement of policy principles for this rule change request.<sup>28</sup>

## D.4 Making electricity rules in the Northern Territory

### Test for scope of “national electricity system” in the NEO

Under the NT Act, the Commission must regard the reference in the NEO to the “national electricity system” as a reference to whichever of the following the Commission considers appropriate in the circumstances having regard to the nature, scope or operation of the proposed rule:<sup>29</sup>

1. the national electricity system
2. one or more, or all, of the local electricity systems<sup>30</sup>
3. all of the electricity systems referred to above.

### Test for differential rule

Under the NT Act, the Commission may make a differential rule if it is satisfied that, having regard to any relevant MCE statement of policy principles, a differential rule will, or is likely to, better contribute to the achievement of the NEO than a uniform rule.<sup>31</sup> A differential rule is a rule that:

- varies in its term as between:
  - the national electricity systems, and
  - one or more, or all, of the local electricity systems, or
- does not have effect with respect to one or more of those systems

but is not a jurisdictional derogation, participant derogation or rule that has effect with respect to an adoptive jurisdiction for the purpose of s. 91(8) of the NEL.

A uniform rule is a rule that does not vary in its terms between the national electricity system and one or more, or all, of the local electricity systems, and has effect with respect to all of those systems.<sup>32</sup>

The Commission’s draft determinations in relation to the meaning of the “national electricity system” and whether to make a uniform or differential rule are set out in chapter 2.

28 Under s. 33 of the NEL and s. 73 of the NGL the AEMC must have regard to any relevant MCE statement of policy principles in making a rule. The MCE is referenced in the AEMC’s governing legislation and is a legally enduring body comprising the Federal, State and Territory Ministers responsible for energy. On 1 July 2011, the MCE was amalgamated with the Ministerial Council on Mineral and Petroleum Resources. In December 2013, it became known as the Council of Australian Government (COAG) Energy Council. In May 2020, the Energy National Cabinet Reform Committee and the Energy Ministers’ Meeting were established to replace the former COAG Energy Council.

29 Clause 14A of Schedule 1 to the NT Act, inserting section 88(2a) into the NEL as it applies in the Northern Territory.

30 These are specified Northern Territory systems, listed in schedule 2 of the NT Act.

31 Clause 14B of Schedule 1 to the NT Act, inserting section 88AA into the NEL as it applies in the Northern Territory.

32 Clause 14 of Schedule 1 to the NT Act, inserting the definitions of “differential Rule” and “uniform Rule” into section 87 of the NEL as it applies in the Northern Territory.



## D.5 Civil penalty provisions and conduct provisions

The Commission cannot create new civil penalty provisions or conduct provisions. However, it may recommend to the Energy Ministers' Meeting that new or existing provisions of the NER be classified as civil penalty provisions or conduct provisions.

The draft rule does not amend any clauses that are currently classified as civil penalty provisions or conduct provisions under the National Electricity (South Australia) Regulations.

The Commission does not propose to recommend to the Energy Ministers' Meeting that any of the proposed amendments made by draft rule be classified as civil penalty provisions or conduct provisions.

## D.6 Review of operation of the rule

The draft rule does not require the Commission to conduct a formal review of the operation of the rule. The Commission may, however, self-initiate a review of the operation of the rule at any time if it considers such a review would be appropriate, pursuant to section 45 of the NEL.

## ABBREVIATIONS AND DEFINED TERMS

2023 IRM Review	Review of the Interim reliability measure, AEMC 2023
AEC	Australian Energy Council
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
Commission	See AEMC
CPT	Cumulative Price Threshold
ESOO	Electricity Statement of Opportunities
EUAA	Energy Users Association of Australia
IRM	Interim reliability measure
IRR	Interim reliability reserve
MPC	Market Price Cap
NEL	National Electricity Law
NEM	National electricity market
NEO	National Electricity Objective
NER	National Electricity Rules
NSW	New South Wales
PoE	Probability of Exceedence
NT Act	<i>National Electricity (Northern Territory) (National Uniform Legislation) Act 2015</i>
Proponent	AEMO
RRO	Retailer Reliability Obligation
USE	Unserved energy
VRE	Variable renewable energy