

10 March 2006

Australian Energy Market Commission
PO Box H166
AUSTRALIA SQUARE NSW 1215



By email: submissions@aemc.gov.au

Re: Rule Change Application – Region Boundary Change Criteria

The ERAA welcomes the opportunity to comment on the revised region boundary change criteria proposed by the MCE. The ERAA is an independent association representing retailers of electricity and gas throughout the National Electricity Market (NEM) and the National Gas Markets. ERAA members collectively provide electricity to over 98% of customers in the NEM and are the first point of contact for end use customers for both Gas and Electricity.

The ERAA welcomes the MCE's proposal to establish efficient criteria for assessing region boundaries in the NEM. The ERAA supports region boundaries that promote efficient dispatch and pricing, and provide appropriate investment signals to generation and loads. Every region boundary adds risk to participants trading in the NEM, and hence a cost of managing that risk. Regions should therefore be minimised within the bounds of economic efficiency. Region boundaries should also allow for the efficient operation of the Settle Residue Auction or other mechanisms to minimise the risk of participants contracting across region boundaries.

The ERAA makes the following comments on the proposed Rule change.

Region Boundary Change Criteria

- The ERAA supports the proposed forward looking economically based boundary change criteria.
- To provide certainty and consistency in boundary change applications, the Rule change application should be amended to require the AEMC to develop, consult on and publish guidelines for the treatment of costs and benefits in an economic net benefits test for a boundary revision. A key issue to be resolved is how the economic benefits attributable to a boundary change will be assessed when it adjoins a region that will change in the next three years. That is the adjoining region has been identified and approved for adjustment via the regional boundary change criteria.

Lead Time

- The proposal attempts to provide stability to the NEM by including a 3-year lead-time for a boundary change decision to take effect, and by preventing review of substantially similar boundaries within a 5-year period.
- This however does not prevent a connection point from experiencing many changes to the region within which it is located within a 5-year period. For example, for a particular region, the decision could be taken to create a new boundary in the northern area of that region thus creating a new region. Then 6 months later the decision could be made to create a new boundary in the southern area of the original region (which is substantially different to the new boundary in the north and thus permitted under the proposed Rule), thus creating another new region. A connection point in the central area of the original region therefore experiences two changes to the boundaries with which it is located within a 6-month period.

- To avoid uncoordinated movement of region boundaries in the NEM, the ERAA proposes that boundary reviews should only be undertaken by an independent body with appropriate technical and market expertise at intervals of 5 years. The ERAA does not support region boundary review by application.
- Region boundary reviews at predetermined intervals also provides the following benefits:
 - avoids the need for the AEMC to manage frivolous boundary change applications; and
 - avoids the complex economic analysis required to compare a boundary change proposal to the future no-change scenario (which could be different from the regional structure of today if another related but different boundary change decision has been made but not yet implemented due to the 3-year lead time).
- The ERAA supports the proposed lead-time of 3 years for a boundary change decision to take effect.

Trigger for Boundary Change

- The ERAA believes that the net economic benefit to trigger a boundary change should be sufficiently high to account for potential errors, poor assumptions, and discretion taken when undertaking an economic test. A boundary change that following implementation did not result in substantial net economic benefit would not only be detrimental to market efficiency, but would also lower market confidence in the AEMC's boundary change decision process. The AEMC should undertake analysis of the economic benefits test for the boundary review and quantify the potential for error. The AEMC should consult with industry and recommend an appropriate level of net economic benefit based on economic analysis.

Procedural Order

- Under the proposed Rule change application, the MCE envisages that a region boundary review could only follow the application of the Last Resort Planning Power (LRPP). The ERAA supports use of the LRPP where it is likely that investment will prove to be economic. However where investment clearly would not be economic, there should not be a requirement for the LRPP to be exercised before a region boundary review can proceed.

Removing Boundaries

- Two adjacent regions with essentially the same (loss adjusted) price provides little efficiency benefit over a single region. However a risk exists contracting between these regions that reduces financial market liquidity. The AEMC should ensure that the benefits of minimising regions are fully accounted for in considering the costs and benefits of a change to a region boundary.

Customer Pricing

- The ERAA does not support the MCE proposal to require the AEMC to consult with the relevant jurisdiction for every boundary change consideration on the issue of managing retail customer pricing implications if a boundary change would create more than one region within a jurisdiction. This has the potential to lead to different pricing solutions in each jurisdiction which increases the complexity and cost for a participant operating in multiple regions.
- If the situation arises where a boundary change would create multiple regions within a jurisdiction, the AEMC should develop a mechanism to manage pricing that would be applied consistently in all regions. This mechanism should be developed in consultation with industry and key stakeholders.

- The cost of managing retail customer pricing has the potential to be significant, and must be fully accounted for in the economic analysis undertaken as part of any region boundary review.

Miscellaneous

Should the AEMC proceed with the MCE proposal for boundary change by application, the ERAA makes the following comments.

- The ERAA questions the need for the AEMC to initiate a boundary review when it identifies material and enduring network congestion. If no participant or NEMMCO believes the benefit from a boundary change would be great enough for it to be worthwhile making an application for a boundary change, it is unlikely that that boundary change would materially benefit the market. Additionally, it was not envisaged when the AEMC was established that they would monitor the NEM at a detailed operational level and therefore would not be well positioned in their own right to determine if a region boundary review is required.
- The ERAA supports the AEMC having the power to reject frivolous applications however suggests that the AEMC clarify on what grounds an application would be rejected (eg. Define material and enduring), and also whether the 5-year period between reviews of substantially similar applications applies to applications rejected by the AEMC.

If you have any queries on the content of this submission, please contact me or Alastair Phillips at ERAA on (02) 9369 4296.

Yours sincerely,

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