

## Congestion Management Program – Statement of Approach

The effective management of congestion is critical to the efficient operation of the National Electricity Market (NEM). Congestion occurs when electricity demand cannot be met using the lowest priced combination of generation available due to transmission capacity or power system security limitations. It would not be efficient to eliminate all transmission congestion, because of the likely cost of doing so compared with the benefits. This means that some congestion, and its management, is inevitable.

Congestion management is necessary to maintain the physical and operational security of the power system and has important implications for spot prices, the degree of competition, the bidding incentives for market participants, and the level of price and volume risk borne by participants. In the long-term, the manner in which congestion is managed affects the investment decisions of new generators, load, network service providers, and the opportunities for alternative energy sources.

The Commission has before it one Ministerial Council for Energy (MCE) reference for Review (Congestion Management Review), and five National Electricity Rule (Rule) change proposals that relate to various aspects of how network congestion is managed in the NEM.<sup>1</sup> It is essential that this work is co-ordinated by the Commission to deliver a comprehensive “Congestion Management Regime” for the market going forward. Predictability in respect of the general direction of the development of the regulatory framework, and confidence that any necessary transitions will be managed, is also essential to those investing in electricity infrastructure. This Statement of Approach is intended to provide information and clarity about the way in which the Commission is going to deal with the five Rule change proposals and the Congestion Management Review in an integrated manner.

The Commission considers that the integrated “Congestion Management Regime” includes all the elements currently under consideration, such as identifying congestion, managing congestion, and setting out appropriate processes for assessing and determining a region boundary change. The “Congestion Management Regime” should be in place for the longer-term, incorporating mechanisms necessary to address network congestion in the short-to-medium term. While the details of these future arrangements are yet to be finally determined, it appears to the Commission that any comprehensive “Congestion Management Regime” is likely to include:

- Information disclosure to the market, such as the NEM Management Company’s (NEMMCO’s) current Statement of Opportunities (SOO)/Annual National Transmission Statement (ANTS) process;
- Incentives to address congestion, such as investment in transmission and generation, and demand-side alternatives;
- Intervention mechanisms such as those relating to price determination, energy dispatch, and /or planner of last resort powers in respect of transmission investment; and
- The potential and process (which itself is clear and stable) for longer-term structural change through the alteration of regional boundaries if this is found to be necessary and appropriate.

The Congestion Management Review, proposed Rules for a revised boundary change process, and the introduction of a last resort planning mechanism have been referred to the Commission by the MCE. These relate to the NEM wide regulatory framework for congestion management and boundary change in the longer term. Two market participant proposals for a short-term change to the current

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<sup>1</sup> These matters are: the MCE-directed Congestion Management Review; Southern Generators/NEMMCO Management of Negative Settlement Residues in the Snowy Region Rule change proposal; MCE Reform of Regional Boundaries Rule change proposal; Snowy Hydro Ltd Review of the Snowy Regional Boundary Rule change proposal; Macquarie Generation Review of the Snowy Regional Boundary Rule change proposal; and Snowy Hydro Ltd. Management of Negative Settlement Residues by Re-orientation Rule change proposal.

mechanisms for managing negative settlement residues at Snowy, and two other market participant proposals to change the Snowy region boundary as a long-term means of addressing existing material congestion in that area, have been submitted to the Commission.

These Rule change proposals, the Congestion Management Review issues paper, and stakeholder submissions on the matters, are available on the Commission's website ([www.aemc.gov.au](http://www.aemc.gov.au)).

The Commission is bound by the NEM Objective when making decisions on these matters, requiring the promotion of efficient investment in, and use of electricity services for the long-term interests of consumers, with respect to price, quality of supply reliability, and system security. When considering congestion and region boundary related proposals, the Commission will have regard to a range of matters and in particular, the impact of the proposals on: dispatch efficiency; facilitation of trading in the NEM, including inter-regional trading; and the promotion of good regulatory practice, including sound regulatory principles regarding the design of the NEM and the National Electricity Rules.

The Commission considers that the issues of congestion management and boundary location in the Snowy region are of more immediate significance than those that currently may arise elsewhere in the NEM, principally because the region sits between the two largest regions in the NEM (measured by MW and MWhs) and because of the particular circumstance that a network loop traverses two region boundaries. The Commission notes that there are "legacy" issues associated with congestion management in and around the Snowy regional boundary that give these matters a priority in the consideration of congestion management and boundary issues in the NEM as a whole. The Commission notes that this view was widely reflected in the submissions received in response to the Congestion Management Review issues paper, the first round consultation for the Rule proposal on managing negative settlement residues in the Snowy region, and the first round consultation on the two Snowy region boundary Rule change proposals.

The current Snowy trial of Constraint Support Pricing/Constraint Support Contracts (CSP/CSC) arrangements is providing an opportunity to assess one option for congestion management, which is not currently part of the permanent design framework of the NEM.

Two of the current Rule change proposals (Southern Generators', transferred to the Commission from the National Electricity Code Administrator on 1 July 2005, and Snowy Hydro's received on 24 May 2006) propose to modify the trial addressing the issue of negative settlement residues in the Snowy region, which would eliminate the need for NEMMCO to restrict flows from Victoria into the Snowy region in order to manage those residues. These two proposals to modify the Snowy trial are each being considered on their merits. The Commission has issued a draft Rule determination proposing to make the Rule change submitted by the Southern Generators and has also commenced consultation on the Snowy Hydro Re-orientation proposal. The Commission proposes to issue a draft Rule determination in relation to the Snowy Hydro Re-orientation proposal in conjunction with issuing a final Rule determination in respect of the Southern Generators' proposal. This will enable the analysis as to the relative merits of the two proposals to be clearly understood. The Commission also notes that the two proposals advocate a different approach to resolve the same problem of NEMMCO's intervention in the Snowy region.

The Snowy trial is currently due to expire on 31 July 2007. If the Commission decides to make the Rules proposed by the Southern Generators or Snowy Hydro (Re-orientation), the Commission would expect that the new arrangements affecting the trial could be implemented by NEMMCO by the start of the coming summer (2006-07), and would expire with the expiry of the trial. That is, the proposals by the Southern Generators and Snowy Hydro (Re-orientation) are short-term in nature.

The Commission anticipates that if it decides to make any of the Rules proposed for a change to the Snowy boundary, implementation may not be practicable before 31 July 2007. That is, the

Commission's decisions on the relevant proposals for changes to the Snowy Boundary are medium-term in nature.

The Congestion Management Review and MCE Rule proposals go to the enduring design of the NEM across all regions. The Commission is currently of the view that any Rules it makes for the short- and medium-term management of congestion and boundary change in the Snowy region should be consistent with the long-term NEM wide framework. Consequently, the Commission intends to co-ordinate its decision making in respect of all of these related matters.

The Commission considers that by adopting this Statement of Approach, the key elements of "Congestion Management Regime" will be announced in draft form by the end of 2006, including the following package of draft Rule determinations and decisions:

- Draft Rule determinations with respect to resolving the Snowy region boundary;
- Draft Rule determination on the future process for boundary changes in the NEM; and
- Draft Report of the Congestion Management Review.

By the end of March 2007, the Commission will release its final Rule determinations on the Snowy region boundary proposals, the future boundary change process, and will submit its final report on the Congestion Management Review to the MCE. It is noted that the final decisions will also have been made on related matters such as Rules for transmission revenue and price regulation, Regulatory Test principles, and a last resort planning mechanism.

By the end of March 2007, the Commission will also clarify transitional arrangements that would be necessary as a consequence of any staged implementation of components of the "Congestion Management Regime" to avoid participant dislocation and disruption to the market. If a decision were to be made to change the Snowy region boundary and implementation of the change was not possible by 31 July 2007 (the expiry of the Snowy trial), the co-ordinated transition process may consider the extension of the Snowy trial (as amended) if necessary, as one possible transition option.

The diagram below shows the Commission's intended approach to its congestion management program.

The Commission considers that it is important for stakeholders to be well informed about the process the Commission will adopt in finalising these inter-related proposals. This Statement of Approach reflects the Commission's commitment to: adopt an open process; be clear about its analytical approach; manage related matters in a co-ordinated and integrated manner; and provide interested stakeholders with the earliest opportunities to understand and respond to issues.

Australian Energy Market Commission  
6 June 2006

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