

Our Ref: M2006/158
Your Ref:
Contact Officer: Paul Dunn
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22 March 2006

Mr Steven Graham
Chief Executive
Australian Energy Market Commission
PO Box H166
AUSTRALIA SQUARE NSW 1215

Dear Mr Graham

AEMC Review into the enforcement of and compliance with technical standards

Whilst much emphasis has rightly been placed on the efficiency of the national electricity market it is equally important that the market reliably deliver energy to consumers. A primary mechanism for achieving reliability is a strong performance standards compliance regime. The Australian Energy Regulator was established under the National Electricity Law with functions which include monitoring compliance with, and enforcing, the Rules which govern the National Electricity Market. A significant component of our activity is monitoring compliance with the performance standards regime that is central to the review the Ministerial Council on Energy has asked you to undertake.

We are pleased therefore to make a submission in response to your issues paper and look forward to working with you towards developing improvements to the current regime. Our submission focuses on key matters of concern to this agency, namely the timely reporting of matters to the AER and the adequacy of the penalty framework. We also have responded in the attachment to this submission to a number of specific questions posed by you. With respect to the balance of the matters raised we consider that industry participants may be better placed to respond.

The AER believes that the Rules should be amended to provide that whenever it has come to the attention of NEMMCO that a registered participant may be in breach of its technical requirements, the AER should, in accordance with a protocol to be developed between the AER and NEMMCO, also be notified of the breach. It would remain the role of NEMMCO to set a reasonable period for the fault to be rectified. Our concern is that all registered

participants should receive the appropriate incentives to speedily resolve any technical non-conformance issue and that the AER has available to it the knowledge base from which trends can be identified and, if necessary, corrective action taken. Under the current arrangement the AER will only be informed of a participant's behaviour when NEMMCO concludes an excessive delay has occurred. Case-by-case this will be an arbitrary and variable period which creates uncertainty and diminishes any emphasis on reliability. We submit the current arrangement contains a risk that it will not provide some participants with sufficient incentive to adequately maintain and repair their plant. Your terms of reference indicate the severe consequences that can flow from technical failures and amply underscores the importance of setting in place active preventative measures to minimise the risk of failure.

Our other major concern is that the current penalty regime does not reflect the level of harm that may be imposed upon others when a technical failure event occurs. In many cases of participant failure where major plant outages have occurred there has been widespread disruption to industry, commerce and to domestic consumers. We cite the event on 14 January 2005 when, as a result of an outage, Queensland participants bore increased ancillary services costs put at around \$800,000 whereas the penalty that was applied was a mere 5% of that amount. We note international trends are to increased penalties, particularly in the US and Korea. We also note that some State and Territory penalty regimes include stronger penalties than those which currently apply in the NEM. It is also pertinent to note that the costs incurred in launching a major enforcement action may be significant. We consider it desirable that the penalty regime strike a balance against those costs.

The AER believes that the penalty which applies in the NEM to a body corporate for a breach of performance standards should be strengthened. At a minimum the AER considers it appropriate to align the penalty with the penalty for rebidding offences under the National Electricity Rules, namely, a penalty of up to \$1,000,000 and up to \$50,000 per day for a breach of the provisions governing performance standards in the NEM. The AEMC may think there is a case for greater penalties to apply. If so, the AER would support a move to increased penalties to improve the general deterrence that results from such an increase.

The AER believes these reforms are essential if the future occurrence of events of the kind that have lead to the current review is to be minimised. We trust your review will address our concerns which are set out in greater detail in the attachment.

Yours sincerely

Michelle Groves