

Dr John Tamblyn
Chairman
Australian Energy Market Commission
PO Box H166
Australia Square NSW 1215

Dear John,

**NEMMCO Participant Derogation (Extension of Cost Recovery of
Regulation Services in Tasmania)**

The existing derogation under Part 11 of Chapter 8A of the National Electricity Rules (NEL) requires NEMMCO to recover the local cost of regulation frequency control ancillary services (FCAS) in Tasmania from participants in Tasmania. In all other NEM jurisdictions, the NER requires regulation services to be averaged across the entire NEM.

The justification for this derogation was as a transitional arrangement between Tasmania joining the NEM on 29 May 2005, and the physical connection of Basslink scheduled for the 30 April 2006. As this has now occurred the derogation should be allowed to expire on the 31 December 2006. Aurora Energy Pty Ltd would argue that the extension of this derogation is unnecessary and on this basis, would be classified as controversial. Accordingly, the current process should be discontinued.

Aurora Energy Pty Ltd would like to make the following comments in relation to NEMMCO's proposal.

1. The existing derogation became part of the National Electricity Code in March 2005 with an expiry date of 31 December 2006, and any proposed rule change in the future is part and parcel of the normal NEM environment. Therefore the degree of regulatory uncertainty is no greater than what would normally be expected as part of any NER Rule Change process.
2. The current arrangements do provide a more accurate locational signal as to the cost of providing regulation FCAS in Tasmania than the alternative, where regulation services are averaged across the entire NEM. However, there is no justification for the Tasmanian region to be treated differently to any other region of the NEM where locational pricing signals are not provided.

3. The principle that parties that bear the cost of regulation services are those that have the possibility of influencing the requirement for the service is fine as an idealistic view. The reality is however that market customers who pay the bulk of the regulation service, due to customer load variability, have limited ability to influence requirement levels and in fact have no control over price. In contrast, market generators on the mainland could influence the cost of regulation services in Tasmania with the co-optimisation process of energy and FCAS across Basslink. The limitations on Basslink to transfer FCAS across the deadband and near the upper and lower limits should be seen as the normal operating constraints associated with the Basslink interconnector within which the market needs to work. In fact, should Basslink approach these limits, the co-optimisation process would ensure that regulation services are imported into Tasmania, if this produced the most economical market outcome.
4. The removal of this derogation and the averaging of regulation costs across the entire NEM would not result in a material impact to market participants.
5. Aurora Energy Pty Ltd would welcome a review by NEMMCO on the effectiveness and operation of the spot market for FCAS.

Based on these observations the existing derogation to localise the recovery of FCAS regulation services in Tasmania should be allowed to expire on the 31 December 2006 without any further extension.

For further details, please do not hesitate to contact Shaun O'Loughlin on 6237 3544 or by email on "shaun.oloughlin@auroraenergy.com.au".

Yours sincerely

Dr Peter Davis
Chief Executive Officer

November 06