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The Chairman
Australian Energy Market Commission
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Dear Dr Tamblyn,

Proposed insertion of a new clause 5.6.5B of the National Electricity Rules to provide the AEMC with a Last Resort Planning Power

The National Generators Forum (NGF) welcomes the opportunity to comment on the Last Resort Planning Power (LRPP) Rule change.

The NGF does not support the LRPP approach as drafted, as it is unlikely to achieve the NEM objective. At least this is because the application of penalties for failure to undertake the test does not distinguish between participant classes or the reasons for the failure to undertake the test. The NGF believes there are alternative ways to address the issue and these are identified below.

Changes in transmission Planning and Investment

The MCE concern which has prompted it to propose the Last Resort Planning Power (LRPP) is that “current arrangements may not deliver timely and adequate levels of transmission investment”. The LRPP is directed at new inter-connector investment and associated intra-regional transmission investment by TNSPs, or jurisdictional planning bodies.

Under the proposed Rule the AEMC will have power to direct a relevant party to undertake the Regulatory test for transmission investment. The reasons provided by the MCE for proposing this Rule are that the current market arrangements and regulatory processes for interconnector development may not deliver timely and adequate levels of transmission investment as:

- “There are no specific requirements that ensure that an inter-regional network investment will be committed¹”,

¹ MCE Attachment A Page 1 - It is assumed that the MCE mean that “There are no specific requirements that ensure that an inter-regional network investment will be subjected to the Regulatory Test.”

- “Inter-regional assets will have a material inter-network impact, a potential investment is likely to require co-ordination between the affected jurisdictional networks which have caused delays to the application of the Regulatory test for what are otherwise economic projects.”²”
- “The Code provided no obligations for network businesses to maintain efficient transfer capacity between regions. There has been no change to this under the transition to the Rules.”³”
- “any inter-regional investment requires a proponent....usually a jurisdictional planning body.”

The MCE also notes that;⁴ “While there should be no Statutory requirement ...the AEMC before directing a party to undertake the Regulatory Test, would identify the failure of the standard process and the cause of the failure. If the causes are for example, due to poor policy settings, then the MCE should be advised in order that the MCE may seek to have that poor policy setting changed, rather than having the last resort planner, direct a party to undertake the regulatory Test.”

The problems that the MCE describes could, in principle, arise in the future. Broadly speaking, the MCE has identified three possible impediments to the development of an identified transmission investment project. In summary these are:

1. the regulatory framework and policy settings for transmission are such that a rational investor has insufficient commercial incentive to invest;
2. the TNSPs or jurisdictional planning bodies are able and entitled to invest, but do not respond rationally to the regulatory incentives, either because of a lack of commercial discipline or because they have other, conflicting, non-commercial objectives; or
3. the project is likely to be uneconomic.

The MCE also notes that for the purposes of clarification:

- The power is not intended to apply to non-transmission projects, ie generation or demand side.”⁵
- “It is expected that the AEMC normally would direct the Transmission Network Service Providers ... given that they have ongoing responsibility for any interregional transmission investment.”⁶, and
- Because, “there may be circumstances (eg a conflict of interest) it is not proposed to restrict the AEMC to only directing TNSPs for the purpose of the LRPP.”⁷

Further we note that in relation to cost recovery the MCE has stated that⁸:

- the AEMC will note that a directed party’s costs incurred in undertaking the Regulatory Test are to be borne by the directed party.”, because “the allocation of costs incurred in undertaking the regulatory test when directed by the AEMC is important for establishing the right incentives for institutions that are responsible for applying the Regulatory test (eg transmission network service providers).”, and

² MCE Attachment A Page 1 - We assume this means that “in the future potential investment is likely to require co-ordination between the affected jurisdictional networks which may cause delays to the application of the Regulatory test for what may otherwise be economic projects.

³ Attachment A - Page 2 – Efficient capacity is determined by the Regulatory Test

⁴ Attachment A - Page 3

⁵ Attachment A - Page 3

⁶ Attachment A – Page 4

⁷ Attachment A – Page 4

⁸ Attachment A - Page 6 - Cost Recovery

- in relation to a failure to comply with a direction within a time frame,⁹ “it is the intention of the MCE that the failure to comply with a direction (under 5.6.5B (c)) from the AEMC when exercising its last resort planning power will attract a civil penalty under the NEL”.

Impact on generators as a class of registered participants

In particular, the NGF is concerned that, (in accordance with the MCE intention) clause 5.6.5B (a) of the proposed last resort planning power Rule allows the AEMC to direct “a Registered Participant” which includes all generators as a class.

It is the NGF’s view that generators should be excluded from being directed because the Rule is directed primarily at correcting for failures of the regulated investment process which, as the MCE proposal notes, could be due to:

- the failure of the TSNP regulatory or policy framework,
- TNSPs or jurisdictional planning bodies that do not behave rationally,
- the TNSPs or jurisdictional planning bodies not undertaking the regulatory test because they believe that the particular investment would not pass the test.

None of these failures are due to any action or inaction on the part of generators, furthermore this is an area where generators are unlikely to have sufficient expertise or resources to carry out the assessment. The inclusion of generators as a class only for the purpose of addressing conflicts of interest is therefore unlikely to be helpful.

In addition the application of costs and penalties to a generator as a Directed Participant will not achieve the MCE objective of establishing appropriate incentives for participants that are in fact responsible for applying the Regulatory test (eg transmission network service providers).

Other ways of addressing the issue are:

- the power to direct should only apply to those Participants undertaking regulated investment, this is consistent with the MCE view that “It is expected that the AEMC normally would direct the Transmission Network Service Providers” , or alternatively,
- if generators are directed to undertake the test they should be compensated with full cost recovery for so doing.

Identification of the failure of the standard process and the cause of the failure.

Also in the case of TNSPs the application of costs and penalties to a TNSP or jurisdictional planning body, where the failure to undertake the test or to invest was due to:

- the failure of the regulatory or policy framework for transmission investment, or
- where the TNSPs or jurisdictional planning bodies correctly did not undertake the regulatory test because in their view the particular investment would not pass the test, would not be appropriate and is unlikely to achieve the MCE objective of establishing the right incentives for TNSPs to drive efficient application of the Regulatory Test.

⁹ Attachment A - Page 6 - Time Frame and Conduct

We note that the MCE has recognised that failure to invest may be as a consequence of policy settings. The AEMC should investigate these potential failures and propose changed policy settings.

In our view, before making a Rule change of this nature the AEMC should:

- be considering *why* a TNSP might be unwilling to promote a potentially economic investment. If it is due to insufficient financial incentives, then this should be corrected through changes to TNSP revenue regulation.
- if the behaviour reflects poor TSNP commercial discipline, allow greater contestability in transmission development.

Both of these potential solutions lie within the scope of the AEMC's current Chapter 6 review and this review should be completed and its recommendations implemented and given time to work before the alternative approach of regulatory direction is finalised.

Conclusion

The NGF does not support the LRPP approach as drafted, for the following reasons:

1. As drafted it does not completely solve the problem. At best, it will make TNSPs submit more projects to the Regulatory Test ("the Test"). This will only lead to actual investment if, a project passes the Test and, none of the other fundamental impediments identified above remain.
2. The application of the proposed Rule to generators would be an arbitrary and ill considered use of the power. Generators should be excluded from the class of registered participants the AEMC may direct.
3. The proposal expands the regulatory powers of the AEMC, in a way not envisaged in the development of the new NEM governance arrangements, and thus increases regulatory risk.
4. Philosophically, it challenges and upsets the established governance principles of AEMC as "rule-maker" and AER as "enforcer" by creating a precedent for the AEMC awarding itself new "executive" regulatory powers on the basis that these promote the NEM Objective.

If you have any questions in relation to this proposal, please call Roger Oakley on 03 9612 2211 or 0408 512 484.

Yours faithfully

John Boshier
Executive Director