

## **Australian Energy Market Commission**

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Review Secretariat  
Department of Industry and Science  
Energy Division  
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**By email:** [energygovrev@industry.gov.au](mailto:energygovrev@industry.gov.au)

Dear Dr Vertigan,

### **Submission to Review of Governance Arrangements for Australian Energy Markets Issues Paper**

The Australian Energy Market Commission (AEMC) welcomes the opportunity to make a submission to the Panel's Issues Paper on the Review of Governance Arrangements for Australian Energy Markets (the Review).

The AEMC considers the governance arrangements have delivered successful market and regulatory outcomes which have been in the long term interests of energy consumers. The proven resilience of the arrangements provides a solid platform for the adoption of potential improvements that further promote successful consumer outcomes from the continuing energy market reform agenda. In this submission, the AEMC has offered some observations on how well the existing arrangements have worked and areas for potential improvement.

The AEMC was formed in 2005 and is the rule maker and developer for Australian energy markets. This includes making rules in relation to:

- the National Electricity Market (NEM);
- the economic regulation of electricity and natural gas transmission and distribution network services;
- wholesale gas markets; and
- the retail sale of energy to consumers and supporting arrangements.

In addition to our statutory rule making responsibilities, we provide advice to, and undertake reviews of market development issues on request by the Council. The AEMC also have the ability to self-initiate reviews into the operation and effectiveness of the rules or any matter relating to the rules.

The AEMC does not set policy in its advice to the Council, but works within the parameters set out in the Council's request for advice, including in the manner in which any policy recommendations are framed. Increasingly, we are also being asked to advise or assist other agencies on issues within their area of responsibilities that impact on energy market outcomes, as reflected in our recent work with the Climate Change Authority and the Department of Environment.

The Council has brought together the Commonwealth, States and Territories to pursue a common set of objectives and coordinate priorities for development of national energy markets.

The way legislative responsibilities for energy are split between the Commonwealth, State and Territory Parliaments has required the Council to be a key institution in the governance architecture necessary to deliver these reforms. The multi-jurisdictional Council model has allowed for the development of a resilient national market framework, facilitated by discussion and agreement on national and jurisdiction-specific policy priorities that support the long term interest of consumers.

Indeed, prior to each participating jurisdiction signing the Australian Energy Market Agreement (AEMA) in 2004, market participants had to deal with different bodies in each jurisdiction – both the regulators and, for gas, the market operators. This was cumbersome, time consuming and costly.

Since the AEMA's signing in 2004, the energy market reform agenda has progressed on a consistent path and has helped to deliver greater choice for energy consumers.

Some of the key energy market reform packages delivered include:

- creation and oversight of the three national energy market institutions (ie, Australian Energy Regulator (AER), Australian Energy Market Operator (AEMO) and AEMC);
- maintenance of stable and effective electricity wholesale market arrangements over time;
- introduction of full retail contestability in electricity and gas across all NEM jurisdictions;
- removal of electricity retail price regulation in several NEM jurisdictions where retail competition has been found to be effective;
- development and refinement of the rules for the economic regulation of network service providers;
- development and implementation of the AEMC's Power of choice review recommendations to provide consumers with more choice in the way they use electricity and manage their bills;
- implementation of the National Energy Customer Framework (NECF) in a majority of NEM jurisdictions; and
- creation of gas Short Term Trading Market (STTM) hubs in Sydney, Adelaide and Brisbane.

The AEMC has established and maintains effective organisational management processes to support transparency through regular reporting to the Council of Australian Governments (COAG), and robust audit and risk management practices. We have documented internal

policies and procedures, which are subject to periodic review and audit, to support our governance model for statutory decision making. There is also an effective budgeting process for review, and approval of, AEMC budgets with the Council.

Overall, there are strong relationships and good strategic discussions are held between the Council, Senior Officials and the three market institutions. This is enhanced by strong working relationships between AER, AEMO and AEMC staff that supports effective engagement and information sharing in the performance of roles, both of which are promoted through Memorandums of Understanding between the market institutions.

As Australian energy markets have become more dynamic, with consumers increasingly driving market developments, it is even more important that the governance arrangements are clearly understood, consistently applied and support market development.

Accordingly, there are a range of opportunities for improvements to be made to the governance arrangements to further embed the effective prioritisation of tasks and for more efficient and effective allocation and completion of work between the Council, Senior Officials and the three market institutions. Potential opportunities for improvement include:

- Council priority setting and management, including transparency of work program outcomes and timelines (see responses to Questions 4, 40, 42);
- the allocation of work across the Council and the market institutions, particularly in relation to alignment with the AEMA (see responses to Questions 5, 22, 39); and
- potentially faster processing of rule changes by the AEMC that remain consistent with the statutory timelines for the rule change process, including the requirements for stakeholder consultation (see responses to Questions 16, 21, 25).

Further information on the achievements of, and potential opportunities for, the governance arrangements for Australian energy markets is provided in our attached detailed response.

If you have any questions or require further information, please do not hesitate to contact me on (02) 8296 7819.

Yours sincerely,



John Pierce  
Chairman

## Section 1: COAG Energy Council

### ***Question 1 — How has (or how do you consider) the Energy Council's performance tracked over time? What factors do you think are contributing to this?***

The Council has brought together the Commonwealth, States and Territories to discuss and pursue a common set of objectives and coordinate priorities for the development of Australia's energy markets.

The development and implementation of a national energy market, particularly in the Eastern States, and the development of the national governance framework are success stories in and of themselves given the varying priorities of different jurisdictions. Furthermore, the consistency with which improvements in economic efficiency and the long term interests of consumers have been pursued across all areas of energy reform, has supported the successful implementation of the Council's reform program. Such consistency helps to provide a degree of policy and regulatory certainty for governments and market participants alike.

Key reform packages delivered include:

- creation and oversight of the three national energy market institutions (ie, AER, AEMO and AEMC);
- maintenance of stable and effective electricity wholesale market arrangements over time;
- introduction of full retail contestability in electricity and gas across all NEM jurisdictions;
- removal of electricity retail price regulation in several NEM jurisdictions where retail competition has been found to be effective;
- the ability to develop and refine in a consistent direction the rules for the economic regulation of network service providers in response to experience and industry developments;
- development and implementation of the AEMC's Power of choice review recommendations to provide consumers with more choice in the way they use electricity and manage their bills;
- implementation of the NECF in a majority of NEM jurisdictions; and
- creation of gas STTM hubs in Sydney, Adelaide and Brisbane.

The Council's ability to deliver effective reforms is dependent on gaining a commitment by jurisdictional governments to the overall benefits to consumers of a national approach and having the structure and processes necessary to deliver it. Where this has been achieved, for example, the creation and ongoing development of the electricity wholesale market arrangements, reforms have been effective and long-lasting.

However, where national reforms are staggered or derogated from across the jurisdictions, success has been more limited. Implementation of the NECF which commenced in 2012 in some jurisdictions, is an example. The NECF was conceived to deliver an effective, uniform consumer protection framework that would provide robust consumer protections while minimising compliance costs for market participants operating across jurisdictions, which

through retail competition would flow through to lower price outcomes. Similarly, there has been limited progress on the development of a national framework for setting distribution reliability standards, and for transmission planning.

The measure of success in the implementation of these frameworks is not that the outcomes are the same across all the jurisdictions. In the example of the reliability standards, a standardised approach would mean that the jurisdictions would set reliability standards using the same economic framework, but the outcomes of the implementation of that framework would reflect the different characteristics of networks and the different preferences of consumers within those networks. This degree of standardisation helps to provide a good quality economic framework for setting the standards, while allowing for regional variations, which has the potential to bring benefits to consumers.

One area in particular where there is potential for all stakeholders to benefit is in greater clarity of the linkages between the Council's strategic objectives and the supporting work program. While all jurisdictions are 'on' the Council, the AEMC would suggest there is scope to increase the degree to which governments 'own' the Council as an institution, its strategic objectives and work program. This matter is explored further in our response to Question 4.

***Question 2 — Should the Panel be contemplating alternatives to the COAG council process for the tasks of leading energy market policy developments? Does the AEMA remain fit for purpose?***

The AEMC has offered some observations in this submission on how well the existing arrangements have worked and areas for potential improvement.

In order to create and implement the NEM in 1998, it was necessary to harmonise laws and regulations governing electricity supply in participating States and Territories. Given the legislative authority over electricity rests with the States, it was necessary to establish an agreement from the jurisdictions to these harmonised instruments.

COAG endorsed a cooperative legislative scheme that allowed one jurisdiction, South Australia, to be the lead legislator for a National Electricity Law (NEL). Each participating jurisdiction signed the AEMA, under which the Eastern States agreed to adopt legislation identical to that of the lead legislature and not to change or repeal the cooperative legislation without unanimous consent. As a multi-jurisdictional body, the Council coordinates and gives direction to the energy market development agenda of State, Territory and Commonwealth Governments.

The AEMC considers the AEMA has been flexible to changes in the reform agenda over time. It has provided the Council with a means to maintain national oversight and coordination of energy policy development and provide national leadership, since it was signed by Ministers in 2004. The Council can consider and incorporate amendments to the AEMA that reflect the Council's evolving energy market reform priorities (eg, NECF implementation) and improvements in methods to obtain more timely and more appropriate market advice (eg, moving from a jurisdiction-by-jurisdiction, to NEM-wide, approach to AEMC retail competition reviews), so as to better meet the long term interest of consumers.

**Question 3 — What are the strengths and weaknesses of the Energy Council's decision making arrangements? Are there examples of specific situations where lack of timeliness, or the need to achieve consensus, has adversely affected market outcomes?**

A strength of the multi-jurisdictional Council model is that it has allowed for the development of a national market framework that has been consistent on its general direction of development and resilient, while evolving over time. The model facilitates discussion and agreement on national and jurisdiction-specific policy priorities that support the long term interest of consumers. It can strike a balance between making it relatively difficult for changes to key elements of previous reforms to be undone, while still allowing for reform as markets develop.

The model, like any multilateral structure, can also have its challenges. For example, it does not always provide timely and nationally consistent market arrangements. Where worthwhile national reforms are subsequently tailored by jurisdictions, administrative and regulatory complexity and associated costs are introduced for market participants who operate across the energy markets. This has been evidenced by NECF implementation, as well as issues such as a common approach to the assessment and setting of distribution reliability standards and for transmission planning.

The current model also raises the potential for ambiguities to develop in the roles to be performed by the Council – that is, Ministers – and Senior Officials which can delay policy outcomes. The Council will generally provide clear guidance on the policy objective, but the detailed implementation elements are then usually developed by Senior Officials and/or their staff.

During this process, there is the opportunity for the Council's original policy intent, and the unity of opinion on that intent, to be diluted. The process can also take a considerable amount of time as all jurisdictions work on the details associated with the terms of reference for reviews or rule change requests (eg, finalisation of Council rule change proposals in response to AEMC recommendations for the Power of choice review (2012) and the Review of electricity customer switching (2013)); also see response to Question 21 for average Council response times to past AEMC review recommendations).

**Question 4 — How relevant is the Energy Council's agenda to contemporary market challenges? How accessible, flexible and transparent is this work program? In what ways might the agenda be improved?**

The Council's agenda, to the extent that the AEMC is familiar with the content of elements of the work program, is relevant for the issues facing the market. The strategic papers that were developed to support the agenda for the December 2014 Council meeting provided both clarity on the issues and transparency of the Council's broad priorities. These priorities were then set out in the Council's published meeting communiqué.

There is the potential to draw a clear linkage or 'line of sight' between the Council's strategic objectives and its work program. One example of how this might occur is by publishing and maintaining the up to date strategic objectives and supporting work program, including transparency in the assignment of tasks and timelines for deliverables, on the Council's website.

Under the new format for Council meetings (as tested at its December 2014 meeting), although the Council's agenda had a good strategic focus, this focus could have been better reflected in the work program which continues to contain a substantial list of what can appear to be unrelated tasks.

Clarity in the articulation of the Council's strategic objectives and its work program (including its purpose), supported by clear public communications of these matters and regular progress reporting against them, is essential for informing and obtaining broad support from stakeholders who are often tasked with implementing policy decisions within specific timeframes. To maintain the momentum of the national energy market reform agenda, including broad stakeholder support, it may be timely to refresh the Council's communications of the national strategic objectives. On an ongoing basis, it is also important to continually draw the linkage between the reform program and the strategic objectives so that stakeholders understand the broader context for change.

***Question 5 — Should the Energy Council meet more regularly or delegate more roles to officials? What suggestions can stakeholders offer to improve efficiency, timeliness and accountability of Energy Council processes, including those of SCO and its key working groups?***

Where the Council's meeting agenda is truly targeted at strategic priorities within a broader reform agenda, the meeting timetable can be appropriate, given the requisite time required by Officials and the market institutions to investigate and publicly consult on priority matters and for Council Officials to coordinate and facilitate meetings.

There is also some flexibility under existing arrangements for 'out of session' decision making by the Council for urgent matters, where required.

Ideally, the Council should set policy and strategic direction, and assign roles to Senior Officials and the relevant market institutions based on the roles set out in the AEMA and a clear set of accountabilities for the delivery of each. Clear timelines and publicly reporting against each action item would also be useful for the purpose of informing stakeholders of progress against the Council's strategic objectives and supporting work program.

***Question 6 — Does the Energy Council provide adequate policy oversight of its three market institutions? Can this be improved?***

The AEMC is accountable to the Council and, as a body established under South Australian legislation, we are subject to, amongst other requirements, audit by the South Australian Auditor General. Our work has national implications because State and Territory Governments have each adopted the national energy laws (and so the national energy rules made under them) as state laws.

The AEMC makes energy rules and provides review recommendations to the Council that will, or are likely to, contribute to the achievement of the three national energy objectives (ie, the National Electricity Objective (NEO), National Gas Objective (NGO) and National Energy Retail Objective (NERO)).

We also have regard to any relevant statement of policy principles issued by the Council in performing our role.

The AEMC's governance framework is different to that of the AER and AEMO, as outlined in the Issues Paper, and hence the relationship and accountability to the Council differs between the market institutions, reflecting their different roles under the AEMA. Any recommendations made by the Panel for the purpose of improving the accountabilities of the market institutions should be made within the context of those differences and with an understanding of the reporting and information currently provided.

The AEMC's strong internal governance framework, with regular reports provided to the Council on the AEMC's work program, budget and a range of other key performance indicators, includes:

- reporting on the size of projects in terms of cost allocation, and how overall costs are tracking against budget; and
- providing updates on the AEMC's work program, budget and strategic financial issues that affect the AEMC at Council meetings.

The information provided in our detailed reporting provides an opportunity for the Council and its Senior Officials to review whether AEMC resources are being allocated in a manner that is consistent with the Council's evolving policy priorities.

Since the start of the 2014-15 financial year, the AEMC has also published an annual Statement of Intent on its website. The Statement of Intent identifies the specific activities that the Council expects the AEMC to undertake in supporting the Council's objectives, and includes key performance indicators for our organisation for which we publish statistics in our Annual Report.

***Question 7 — What should be the Energy Council's role in areas outside its direct policy remit, including financial markets, sustainability and climate change issues and social policy? What role should it take in engaging with non-interconnected states like the Northern Territory and Western Australia? What role should it take in areas beyond its AEMA coverage, such as retail price regulation and technical and safety matters? What practical barriers might need to be addressed in its taking on such roles?***

The Council has an energy policy leadership and information dissemination role to play by undertaking and commissioning work to investigate matters that have a potential impact on the long term interest of energy consumers. That said, in order for the Council to perform its core energy policy functions and responsibilities well, it needs to be mindful of any potential impacts on, or interactions with, other policy areas.

Where there are policy issues that will impact on the Council's energy market reform agenda, the Council could take a role in leading and commissioning work to understand the impact of policies being considered outside the energy portfolio, on the energy sector. This has the potential to promote integrated and consistent policy outcomes.

The Council could leverage the expertise of the market institutions to help with these issues.

In AEMC reviews, to the extent possible, we undertake consultation with parties with whom there is potential for cross-over on issues as part of our work, and we highlight such issues and possible options in our reports to the Council for it to consider the next steps.

Increasingly, we are also being asked to advise or assist agencies outside the energy

portfolios on issues that impact on the sector, as reflected in our work with the Climate Change Authority and the Department of Environment.

We note that, as members of the Council, the non-interconnected jurisdictions of Western Australia and Northern Territory have an opportunity to contribute to, and be informed of, the national energy market reform agenda. Recent developments in these jurisdictions toward greater regulatory alignment with national rules and the roles performed by the national market institutions demonstrate that current Council arrangements appear to be working well.

## Section 2 — Australian Energy Regulator

### ***Question 9 — Does the concept of a national energy regulator, separate from the rule maker and jurisdictional governments, remain relevant in today's market? Should the Panel be considering alternative models***

Institutional structures need to be derived from a framework or set of principles that recognise that for institutions to be effective, their functions and governance arrangements need to be consistent with Australia's particular federal structure of government.

There needs to be consistency between the allocation of legislative responsibilities between levels of government and the governance arrangements. This needs to be explicitly considered in the case of the energy sector where national market arrangements operate in an area of state legislative responsibility.

The AEMC is an example of a national, independent organisation operating in an area of state government responsibility. The broad and inclusive approach to rule changes and reviews under the current institutional arrangements means that changes in energy market arrangements are considered against the legislated national energy objectives, taking into account policy objectives, commercial and financial impacts on participants and technical issues in a coherent way. An explicit focus on the long term interests of consumers in developing new rules, rather than on the potential for a range of ambiguous and conflicting objectives to influence outcomes, has contributed to greater regulatory predictability and transparency of the rule making process.

The separation of regulator from rule maker is not that unusual across international energy markets. In many countries, regulations or rules are developed by government, while regulators apply the rules and develop binding guidelines or other operational or compliance-related instruments. In the Australian context, the energy legislation is broad by necessity, given our federal structure and partial split of responsibilities between federal and state governments, and much more of an enabler. This allows the rule making process managed by the AEMC to be more detailed, transparent and reflective of changing market dynamics.

The rule making role of the Commission is also compatible with its other function, namely the provision of advice on market development to the Council. It is generally difficult to find examples, either in Australia or internationally, where a market institution is both an adviser to government or rule maker, and enforcer of the rules and regulations. Even where this may be the case, the nature of the checks and balances in place where power is concentrated in this way need to be understood to effectively evaluate the approach. At its most basic, combining the AEMC and AER would be akin to having Parliaments, rather than the Courts, enforce laws made by Parliaments. Or another way of looking at it, it would be akin to having the police, and the Australian Federal Police at that, determining state level legislation and regulations.

***Question 16 — How could the relationship between the AER and the other two market institutions (AEMC and AEMO) be improved? Should the AER be given increased capacity to help develop expedited rule changes, or an increased role in reviews or policy advice?***

Relationships between the AER and the AEMC are well developed. Examples include regular meetings between the AER Board and AEMC Commissioners, as well as regular meetings between the senior management teams. There are also strong working relationships at the staff level, which has been promoted through regular engagement and cooperation on the analysis of issues arising from rule change requests (eg, obtaining AER views on any rule enforcement issues when drafting rules) and market reviews (eg, notification and sharing of information that may be relevant to either organisation, in accordance with our published Memorandum of Understanding).

Energy laws currently allow the AEMC to fast-track a rule change request from other institutions. A rule change submitted by the AER or other market body, including AEMO, the Reliability Panel (for the NEL only) and some specific gas market regulatory bodies (for the National Gas Law (NGL) only), can be considered for this process.

There are currently conditions, however, under which the AEMC can exercise this fast-track option for rule making. The AER and AEMO (by way of example) must have consulted with the public on the nature and content of the rule change request and the AEMC must be of the opinion that such consultation has been adequate.

Fast-tracking is designed to prevent duplication of consultative processes. There have been very limited opportunities for the AEMC to use this process, either as a result of previous consultation on the nature and content of the rule change request, or reluctance by the rule change proponent to utilise the fast-track process for rule making.

***Question 18 — Are there opportunities to improve confidence in regulatory outcomes, for example through improved communication or performance and accountability measures?***

As noted in our response to Questions 4, 40 and 42, clear public communication of the Council's priorities and areas for market development, including regular progress reporting, is essential for informing and obtaining broad support from stakeholders, including energy businesses, who are often tasked with implementing or working with the outcomes of policy decisions.

### **Section 3 — Australian Energy Market Commission**

***Question 19 — How has (or how do you consider) the AEMC’s performance tracked over time? What factors do you think are contributing to this?***

The AEMC is 10 years old this year. In the past decade, our national energy market responsibilities have evolved in the following way:

- the AEMC was formed in 2005, after the decision to split the National Electricity Code Administrator’s (NECA) responsibilities for managing change processes and compliance in relation to the National Electricity Code;
- since 2005, the AEMC has been responsible for electricity rule making and market development under the NEL;
- in 2008, under the NGL, the AEMC’s role expanded to include the economic regulation of electricity distribution network services, gas transmission and distribution services, and natural gas pipeline access;
- in 2009, our role expanded to include gas retail functions and Victoria’s declared wholesale gas market, with the STTMs for gas added in 2010; and
- in 2012, under the National Energy Retail Law (NERL), the AEMC assumed responsibility for the National Energy Retail Rules (NERR) as part of the Ministerial Council on Energy’s NECF package of reforms, further extending our rule making functions to include electricity, gas and energy retail rules.

In 2006-07, the AEMC had 32 active rule change proposals under consideration, made 14 new rules and completed 2 reviews. Since that time, we have continued to develop the quality of our documents and particularly our analysis framework, with the addition of expanded economic analysis and communications capabilities.

The sophistication of our communications function has increased significantly with more accessible information and more varied tools to engage with a range of stakeholders and, importantly, consumers. In 2013-14, we held 531 stakeholder presentations and meetings, compared to 258 in the previous year, reflecting both our increased engagement focus and stakeholders’ greater interest in engaging with us.

In 2013-14, the AEMC had 22 active rule change proposals under consideration, made 17 new rules and completed 14 reviews.

***Question 20 — To what extent does the AEMC’s statutory rule making process remain appropriate in today’s market? Should the Panel be considering, for example, returning this role to jurisdictions or to the Energy Council?***

In order to answer this question, it is useful to understand the governance framework that existed prior to the creation of the AEMC and the AER.

Table 1 outlines how elements of the energy markets were regulated prior to the national governance framework, and how this has changed with the implementation of the national governance framework.<sup>1</sup>

A number of different bodies were making rules while jurisdictional regulators were undertaking economic regulation of network services, along with the Australian Competition and Consumer Commission (ACCC), utilising different regulatory approaches.

Rule making through legislative process tends to be less responsive to market developments compared to the process utilised by dedicated rule making institutions.

In many cases, there was no separation between the rule maker and the enforcement body – for example, in Victoria and South Australia, the regulators were making and enforcing instruments such as retail consumer protection codes.

Market participants had to deal with different bodies in each jurisdiction – both the regulators and, for gas, the market operators. This was cumbersome, time consuming and costly.

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<sup>1</sup> Some areas are still subject to specific jurisdictional forms of regulation. For example, non-economic regulation of distribution networks still largely rests with the jurisdictions.

**Table 1: Australian energy markets governance framework, pre and post AEMA**

	Pre - AEMA			Post - AEMA		
Electricity	Rule maker	Application	Enforcement	Rule maker	Application	Enforcement
Operation of markets, system security and related functions	NECA & ACCC	NEMMCO	NECA	AEMC	AEMO	AER
Economic regulation of transmission services	ACCC	ACCC	Judicial review	AEMC	AER	Merits/judicial review
Economic regulation of distribution services	Jurisdictional regulators <sup>2</sup>	Jurisdictional regulators	Judicial review	AEMC	AER	Merits/judicial review
Retail – licensing, consumer protection, and retailer-distributor relationships	Jurisdictional regulators, Parliament or Minister		Jurisdictional regulators	AEMC		AER
<b>Gas</b>						
Operation of markets, system security and related functions (to the extent not undertaken by the networks)	Jurisdictional market operator <sup>3</sup>	Jurisdictional market operator	Jurisdictional regulators	AEMC	AEMO	AER
Economic regulation of transmission services	ACCC	ACCC	Judicial review	AEMC	AER	Merits /judicial review
Distribution – economic regulation of services, including retailer – distributor relationship	Jurisdictional regulators <sup>4</sup>	Jurisdictional regulators	Judicial review	AEMC	AER	Merits/judicial review
Retail – licensing and consumer protection	Jurisdictional regulators, Parliament or Minister		Jurisdictional regulators	AEMC		AER

<sup>2</sup> For example, IPART, ESCOSA, ESC of Victoria. Generally exercising and applying fairly general laws, with a large amount of discretion.

<sup>3</sup> For example VENcorp in Victoria and Gas Market Company in NSW.

<sup>4</sup> For example, IPART, ESCOSA, ESC of Victoria. Generally exercising and applying fairly general laws, with a large amount of discretion.

Recognising the important policy role for governments, in 2001, COAG established a new Ministerial Council on Energy (MCE) to provide policy leadership to the energy sector and the means for participating jurisdictions to coordinate on important energy policy issues.

At the time, there was a general level of concern with the governance arrangements, in particular, with NECA's role versus the MCE's in terms of policy setting. Additionally, there was potential for regulatory overlap due to a lack of clarity in roles and responsibilities between institutions, often leading to duplication in consultation processes between the ACCC (ie, the competition regulator) and NECA (ie, the manager for change processes and compliance in relation to the National Electricity Code, with breaches being referred to the National Electricity Tribunal).

COAG subsequently commissioned an independent review of governance arrangements: the Parer Report (2003). In light of the Parer Report's recommendations, the MCE recommended to COAG that NECA be abolished and two new statutory bodies be established:

- the AEMC replaced NECA as the rule maker and was provided with an additional function of market development adviser to the Council; and
- the AER replaced the ACCC as economic regulator and NECA for rule compliance.

The new NEL set out the roles and functions of the AEMC and AER, and the National Electricity Code was changed to the National Electricity Rules (NER).

The focus of the new governance arrangements was to bring greater clarity to the roles and objectives of the governance institutions, and to separate rule making and market development advice from rule enforcement and compliance.

A key feature of the new arrangements was to consolidate a range of different market objectives into a single National Electricity Objective linked to the long term interest of consumers of electricity. The new arrangements also provided for a single process for developing rules, in contrast to the previous two-tiered approach which required both NECA and the ACCC to review changes proposed by participants. Also, governments determined that it was not appropriate to seek authorisation by the ACCC of rule changes under Part IV of the Trade Practices Act 1974 (Cth).<sup>5</sup> This was a significant decision.

The NEL (as well as the NGL and NERL) enables any person, apart from the AEMC, to initiate a rule change proposal<sup>6</sup>, including industry participants, other institutional bodies, end users, as well as the Council. Previously, only NECA and industry participants (with agreement from at least six participants) could submit rule change proposals. It is important to note, however, that these new arrangements did not remove any law making functions from any Parliament. The AEMC largely took on the rule making functions that had been undertaken by jurisdictional regulators or technical bodies.

We note that under the new arrangements, the Council is able to initiate rule changes without AEMC involvement and, given the broader mandate of the Council, this is completely appropriate.

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<sup>5</sup> Renamed the Competition and Consumer Act 2010 (Cth), effective 1 January 2011.

<sup>6</sup> Limited restrictions exist under the NEL in relation to who can submit rule change requests affecting AEMO's declared network functions and derogations.

The new framework allows significantly enhanced participation from a range of stakeholders, including consumer groups, in the rule making process. Importantly, the AEMC is not empowered to initiate rule changes, other than to correct minor errors or where the proposed change is non-material. Instead, the AEMC's role is to manage the rule change process, and to consult and decide on rule changes proposed by others. The new arrangements consequently impose a strict level of policy control, which is the province of the Council, on market developments and establish well understood and transparent processes for policy and regulatory changes.

While the current approach to rule making can take time, because of the level of stakeholder engagement, it also leads to better regulatory decision making and minimises the risk of inappropriate decisions being made. An independent decision making body, separate from industry and government but with a clear and consistent objective, is able to determine rules that best align with the policy intent and governments' broader reform agenda.

A considered and consistent approach to reform is desirable as inappropriate regulatory or policy decisions inevitably have significant consequences for markets, undermining confidence in those markets and in the institutions that govern them. This can cause momentum for reform to slow or even retreat. The current institutional arrangements and processes minimise the potential for this to occur, ensuring a self-sustaining framework for ongoing market reform.

As noted above, the Council can make rules without proposing them to the AEMC first, although we believe there are significant benefits in not doing so. For example, the Council can highlight its key policy imperatives and rationale for proposing such a change, and the current rule making process incorporates extensive public consultation and is a process that is generally understood by energy stakeholders, including consumers. In addition, in terms of the scale and speed of the energy market reform agenda, governments can maintain an appropriate degree of influence over the overall size of the AEMC, which complements the inherent flexibility in the AEMC's structure to respond to an expansion of its functions (eg, added rule making responsibility for the NERR in 2012).

We are of the view that the current rule making arrangements have largely worked and been managed well, and in the long term interest of consumers. As always, however, there is scope for improvements and we make some proposals in this submission that could further improve the rule change process (see response to Question 25).

**Question 21 — Do you consider there are any issues in relation to the performance of the AEMC's functions? To what extent are your views on the performance of the AEMC due to its institutional arrangements, resourcing, the process requirements for rule making, or other factors? To what extent does the AEMC's governance contribute to how it exercises its statutory rule making and market development function? To what extent do you consider the AEMC's rule making processes are achieving the national energy objectives of serving the long term interest of consumers? To what extent are your views a function of its institutional arrangements, the legislative framework it operates in, resourcing, or other factors?**

The AEMC has two functions:

- it makes and amends the national electricity, gas and energy retail rules; and
- conducts independent reviews for the Council, including the ability to self-initiate reviews into the operation and effectiveness of the rules or any matter relating to the rules.

The statutory processes for rule making which are defined in the national energy laws, and the terms of reference for AEMC reviews which we publish on our website, serve an important purpose for all interested parties. They define the overall process and approach to a project, set dates for the key deliverables, and most importantly, make provision for stakeholder consultation. To do this effectively with a broad stakeholder group takes time, particularly for detailed technical issues or major reforms. We are acutely aware of the timeframes within which our work is delivered, and we balance the delivery of effective review recommendations and robust rules against the mutual benefit that is derived from active and informed stakeholder debate.

The AEMC's rule making processes are enshrined in national energy laws. The rule making test that we apply, and must follow under law, for all rule change requests under consideration is whether making a rule will, or is likely to, contribute to the national energy objectives, which serve the long term interests of consumers. Our reasons for making (or not making) a rule, including how our decision serves the long terms interests of consumers, is published in the final rule determination for each rule change request on our website. Our decisions are also subject to judicial review.

The laws make provision for standard, expedited (for non-controversial or urgent rules) and fast-track (for market regulatory bodies/review related) rule making processes. Public consultation is a feature of all these rule making processes. The laws also afford some flexibility to the AEMC to make a more preferred rule to the one proposed where it better meets the national energy objectives, and for the AEMC to consolidate two or more rule change requests where the AEMC considers it necessary or desirable to consider the requests together.

To help stakeholders understand the statutory rule making process and rule making tests (ie, contribution to the national energy objectives), we openly discuss these matters with prospective rule change proponents in general day-to-day communications, in addition to publishing guidelines on our website (including for the fast-track process) which explain how to prepare rule change requests prior to lodgement with the AEMC.

The time required to make effective rules is driven by the complexity of the issue and the degree of stakeholder interest in the issue. Our process allows for consideration of relevant

issues, extensive stakeholder consultation, development of a robust rule design, and seeks to minimise the risk of inappropriate decisions being made which could adversely impact on confidence in market arrangements.

We seek to make enduring rules that provide high level guidance but are sufficiently prescriptive, providing a framework for detailed technical matters to be articulated in supporting procedures. For example, by making rules that requires AEMO to develop procedures for retail gas markets, or the AER to develop guidelines for network regulation. This approach seeks to ensure that the rules are flexible enough to accommodate the changing needs of the market over time without continued regulatory intervention for minor matters, empowering affected stakeholders to consider and improve technical and supporting processes, as appropriate.

We are aware of some stakeholders' desire for us to make rules faster and, generally, in less than six months. For less complex rule change requests, we are investigating processes that could facilitate faster rule making, but would also appropriately manage the public consultation trade-off that is valued by stakeholders (see response to Question 25). For more complex rule change requests, such as the Council's proposed changes for 'Expanding competition in metering and related services' (2014), there may be justifiable reasons to extend rule making timeframes, as permitted under the energy laws, so as to facilitate better rule making design and sufficient public consultation.

To improve public transparency of our processes, we have articulated a set of key performance indicators for monitoring our rule change performance in our Statement of Intent and publish related performance information in our Annual Report.

In terms of our market development function, we have conducted independent reviews in response to requests from the Council, and have self-initiated reviews where we have believed there to be issue (eg, the AEMC's gas scoping study (2013)). The energy retail competition reviews have transitioned over time from a jurisdiction-by-jurisdiction approach, to an annual NEM-wide approach in response to the progressive removal of energy retail price regulation by jurisdictions.

In our reviews, where we have identified deficiencies in the operation of rules, we have made policy recommendations to the Council for it to consider and propose in the form of a rule change (eg, the AEMC's Power of choice review (2012)), as we generally cannot initiate rule changes. We are aware of a perception held by some stakeholders that this process unnecessarily extends the time period before words (policy recommendations) are converted to action (rules), particularly where analysis and consultation has already occurred as part of a completed review.

In some cases, particularly for relatively minor matters that have been identified as potential areas for reform through a rule change, there may be some merit in stakeholders' views that the rule making process is longer than it needs to be. However, in general, matters that are considered in reviews are not trivial. They may involve multiple rules, affect multiple and diverse stakeholders, or have a non-energy policy component, such as understanding the potential consequences for financial markets in response to the failure of a large market participant. The review timeframe may not accommodate investigations of all the issues necessary to convert a policy recommendation into detailed rules drafting. In addition, policy makers require time to properly consider our recommendations.

For example, we have investigated past AEMC reviews that we have undertaken on request by the Council, and which have resulted in subsequent reviews and rule changes in response to our review recommendations. It generally takes the AEMC around nine months to complete a review (ie, from receipt of the terms of reference, to provision of the final advice). It can then take another eight months for the Council to respond to the review recommendation.

This implies that it generally takes about 17 months before the AEMC considers a rule change request or request for further advice from the Council in response to a recommendation that the AEMC has made in a review. This has implications for the currency of stakeholder issues considered as part of previous AEMC reviews when considering the subsequent rule change request. Some potential opportunities for more timely rule change assessments are discussed further in our response to Question 25.

Our work program is driven by external stakeholders, either through stakeholders lodging rule change requests, or Council requests for advice on specific aspects of the energy market. Accordingly, we need to carefully balance our work program against our available resources (both human and financial). We do this by proactively engaging in a dialogue with external stakeholders, including AEMO and the AER, to identify and understand emerging market issues and their urgency. This informs and helps us to prioritise projects, better manage resources and set stakeholder expectations.

For example, in May 2014, we held our first strategic priorities forum with consumer representatives in order to deepen our relationships as we consider the agenda ahead of us for energy market development. The strategic priorities form the basis of our market advisory role and are reviewed periodically through a process of public consultation. Together with consumer, industry and government stakeholders, we are solidly engaged on market-wide issues which extend our daily, project-specific consultation.

The AEMC has documented internal policies and procedures, subject to periodic review and audit, to support our governance model for making statutory decisions.

The Commission meets formally at least weekly to consider statutory rule changes and reviews, and monthly to consider organisational management issues and reports. Statutory decisions are made by at least two out of our three Commissioners (1 full time Chairman, 2 part time Commissioners), who are operationally supported by AEMC staff and led by a Chief Executive. Delegations to the Chief Executive and senior managers to support efficient AEMC decision making and operations exist, as appropriate, and are regularly reviewed in light of the continuing energy market reform agenda.

Routine and regular non-statutory internal policy discussion meetings are held with Commissioners, to highlight pertinent issues arising from stakeholders' submissions to our public consultation processes and to agree on a consistent and integrated approach for certain policy matters, prior to the making of statutory decisions.

**Question 22 — To what extent do you consider it is important to have an independent market development role within the AEMC? To what extent do you consider the AEMC's market development role 'outsources or augments' the policy responsibilities of the Energy Council? Does the market development role of the AEMC 'outsource or augment' the technical input to policy provided by the AEMO and AER? Are there alternative recommendations the Panel could pursue to improve collaboration in market development, and/or policy oversight by the Energy Council? To what extent is it important to clearly define the scope of the AEMC's 'market development' role, and the demarcation between the Energy Council and other institutions?**

As noted in our earlier response to Question 2, in order to operate the NEM, it was necessary to harmonise laws and regulations governing electricity supply in participating States and Territories. Given the Commonwealth lacked explicit legislative authority over electricity, it was necessary to get an agreement from States and Territories to these harmonised instruments. At the same time, under a multi-jurisdictional arrangement, it is necessary to have some centralisation of the market development function and advice.

The AEMC is independent of sectoral interests. The Council's involvement in the AEMC's operations is generally limited to the provision of requests for advice. These arrangements maintain the AEMC's independent rule maker role, the risk being that sectoral interests' involvement in rule making decisions (other than through making submissions to open and transparent public consultation processes) could lead to a perceived or actual conflict of interest.

The AEMC's market development functions are fulfilled by the provision of detailed advice to the Council, either requested by it, or initiated by the AEMC in relation to the operation and effectiveness of the rules or any matter relating to the rules.

The AEMC does not set policy in its advice to the Council, but works within the parameters set out in the Council's request for advice, including in the manner in which any AEMC policy recommendations are framed. While the analysis and consequent recommendations in relation to that analysis could be considered as being 'outsourced' to the AEMC, the purpose of our work is to inform the Council so that it is in a better position to make policy decisions that support market development.

The alternative would be either that Government departments would have to grow to develop this expertise, or each department would have to access that expertise individually which would necessitate the need for an institutional structure staffed by all the Governments to make decisions.

As it is the national rules that give effect (or 'life') to the Council's policy decisions, it is appropriate for the market development function to reside with the rule maker. This assists with a coherent and consistent approach to policy implementation and limits the potential for influence from market participants other than through public consultation processes.

With Council oversight, collaboration between the market institutions in market development is likely to be optimised where all parties have a clear understanding of their respective roles, accountabilities are clearly assigned, and regular reporting and communication lines are promoted by all parties. To the extent that the Council considers it appropriate for a market institution to deviate from its defined role (eg, by way of the Council issuing a terms of reference for advice on a specific matter), it may be helpful to stakeholders for the reasons for the deviation to be explained by the Council. The risk of not doing so is the

potential for market participants and consumers to become confused on whom, and how, to engage with effectively on issues they regard as important to them.

Our market development work, through the provision of advice to the Council and published reports on our website, also serves to inform and facilitate greater engagement with the AER and AEMO in related technical areas.

***Question 23 — To what extent does the AEMC’s commissioner structure, and the split between Commonwealth and States and Territories membership, affect its capabilities and approach to its rule making and market development tasks? Are there alternative oversight models the Panel should consider, for example a board structure or additional commissioners?***

The effectiveness of the AEMC’s governance arrangements is derived from there being a clear ‘line of sight’ and consistency between the following key elements:

- level of government with legislative responsibility for the stationary energy sector;
- scope and clarity of the functions the AEMC is given responsibility for;
- appointment processes for Commissioners, and that the Chief Executive is appointed by, reports to and is accountable to the Commission;
- reporting and accountability mechanisms to the Council for how the AEMC is managed and how it performs its functions; and
- source of funding.

It is the consistency of each of these elements with one another that leads to the AEMC being ‘owned’ by all governments and having an interest in how it performs. It also gives it its national, as distinct from Commonwealth, status.

AEMC Commissioners are appointed on merit, rather than to represent a particular constituency or sectoral interests. Independence in decision making from the appointing States and Territories (and the Commonwealth) is also supported via the application of the legislated national energy objectives to statutory decision making processes for rule making and market development tasks.

A robust and transparent approach to disclosure of interests is essential to preserve the integrity of the AEMC’s decision making and to ensure that people with energy sector experience and knowledge are available to serve the Commission. By law, the AEMC and the Commissioners are required to identify, disclose, record and manage any conflict of interest. The AEMC has established processes to put into effect these requirements, including cases where it is possible that a perception of a conflict of interest might arise. The AEMC has a policy of open disclosure regarding arrangements by each of the Commissioners for the ongoing management of conflicts of interest.

The current model works well because of the open disclosure policy the AEMC has applied and the regular policy briefings the jurisdictional governments receive through the Council. If, for example, a statutory board rather than Commission structure was considered appropriate for the AEMC, operationally, this is unlikely to have any significant internal impact as the Commission generally tends to function in this manner on a day-to-day basis. As noted

earlier, we are required under law to identify, disclose, record and manage any conflict of interest, as would a statutory board.

In the future, the AEMC's rule making and market development roles may be enhanced, for example, by increasing the number of AEMC Commissioners. Any increase would need to be consistent with the scale and breadth of our statutory role, and balanced against reasonable opportunities for Commissioners to make informed and effective statutory decisions in other ways (eg, through greater use of Commission sub-committees with full decision making delegations).

In recent years, there have been increasing demands on the three Commissioners' time from internal and external stakeholders, as well as a broader scope of issues with the NERR added to our NER and National Gas Rules (NGR) rule making functions. We have been managing these demands through greater internal delegation, subject to appropriate oversight and risk management procedures, and streamlining of internal processes. However, our relatively flat organisational structure means there are limits in terms of the extent to which we can delegate managed risk down through the organisation.

Accordingly, while the current (1 full time, 2 part time) Commissioner arrangements are working appropriately at this point in time, we consider this Review represents an opportunity for the Panel to consider ways in which the AEMC's establishment legislation could be amended to allow for the appointment of additional Commissioners (either full or part time) in response to the variability or increase in the Commission's workload.

***Question 24 — Do you consider the AEMC is adequately resourced to undertake its roles? Should the AEMC be funded by market participants or cost recovery, rather than being on budget from the States and Territories? Does it have the right skills base to undertake its functions, particularly across the spectrum of electricity, gas and retail sectors?***

The AEMC is adequately resourced to perform its roles of rule maker and market developer.

We are allocated funding with jurisdictional oversight, with three-year rolling budgets based on annual reviews to adjust for budget 'unders' and 'overs' given past and upcoming workload. Any funds not used are returned to the jurisdictions, including \$1m this year.

Given that we make rules and conduct reviews for the Council in support of the national energy objectives, sourcing our funding from state governments is important in that it directly aligns with our accountability to jurisdictions as members of the Council and serves to manage any perceived conflict of interest from industry or other sectoral interests in the performance of our role. It is a matter for Governments as to how they obtain such funds (ie, consolidated revenue or levies on industry or consumers). We understand that Governments adopt a range of approaches to raise their share of the AEMC's budget.

The AEMC employs a mix of professionals from diverse and relevant backgrounds including, economists, lawyers and engineers drawn from the public, private and non-government organisation sectors that enables the AEMC to meet its rule making and market development functions. To help our teams to communicate more effectively with consumers, the AEMC also employs a small number of communications professionals. In addition, the AEMC is supported by a corporate services team specialising in finance, human resources, information technology and administration, to keep the organisation functioning each day.

To the extent that the AEMC requires highly specialised skills for the purpose of informing our rule change or market development work, such as market modelling, we also maintain a panel of consultants who have pre-registered their skill sets with the AEMC, enabling us to quickly draw upon their skills through appropriate procurement processes.

***Question 25 — What are the opportunities to improve the timeliness of rule change assessments? For example, should there be a faster track for rules which arise out of reviews by the AEMC or other reputable bodies, or should the AEMC be able to progress less well refined rule proposals from the Energy Council or market participants or have some flexibility to initiate its own rule change proposals? What other opportunities are there to improve the accessibility, transparency, and rigour of the AEMC's processes?***

Generally speaking, when stakeholders, including Governments, consider that an aspect of the national energy rules could be improved and they are reasonably clear about how this should be achieved, they submit a rule change proposal to the AEMC for consideration. When Governments, perhaps informed by stakeholders' views, have concerns about a particular issue, but have not yet developed a clear view as to how best to address the issue, they can ask the AEMC to undertake a review.

In general, there are two types of AEMC reviews:

- reviews that are broad in scope and tend to cover multiple issues (eg, the Power of choice review (2012), and the Transmission frameworks review (2013)); and
- targeted reviews aimed at addressing specific or contained issues (eg, reviews that focus on operational or system improvement matters, rather than broad policy questions, such as the Review of electricity customer switching (2013)).

Both types of reviews often result in the submission of recommended changes to the rules for Council consideration. As outlined earlier, it generally takes the AEMC 9 months to conduct a review<sup>7</sup> and the Council then spends about the same amount of time considering the recommendations before formally submitting a rule change request.<sup>8</sup>

The AEMC has been investigating opportunities to reduce the time this overall process takes while still providing sufficient time for effective consultation, robust analysis and considered decision making. We have considered these opportunities in the context of a 'staged review and rule making' approach, and in a 'single step response to an AEMC review' approach, as outlined below.

These opportunities for more timely rule change assessments go beyond our long-standing process for publishing a consultation paper with the rule change proposal at the start of the rule change process, which helps to provide context for stakeholders, particularly consumers, and focus stakeholders' attention on the key issues that have been identified early in the process. We note the following four opportunities, the latter two of which we are more readily employing in our day-to-day operations.

<sup>7</sup> This is a typical time period and the actual length of reviews has varied significantly from a few months to a number of years.

<sup>8</sup> As with the time it takes the AEMC to undertake reviews, this is a typical length of time for Council response, and the actual length of time for response has varied from a few months to a number of years.

(i) Staged review and rule making

The purpose of this approach in these broad types of reviews is to provide an appropriate checkpoint for the Council after the AEMC completes the first stage of a review. This allows the Council to consider the analysis and confirm the need and scope for the second stage of the review prior to its commencement. This approach would also enhance the division and transparency of responsibilities for policy development between the Council and the AEMC.

The approach would work as follows:

- Stage 1: the AEMC considers the problem, analyses the options and makes recommendations to the Council on the further market development requirements. The AEMC seeks Council input on its recommendations.
- Stage 2: Upon agreement from the Council, the second stage would consider implementation issues, including development of rules (and other instruments, if required).

Upon receipt of the Stage 2 report, if the Council was able to submit a rule change proposal to the AEMC within six months of receipt of the report, the AEMC would then commit to having the rule change completed within six months. Given the Council has had the opportunity between Stage 1 and Stage 2 to assess the merits of the policy direction and agree to the rule change requests, it is expected that the subsequent decision making time required after Stage 2 can be shortened. However, we recognise that there will be circumstances in which the Council wants to take longer to consider AEMC recommendations.

In turn, a quicker response from the Council would allow the AEMC to rely on stakeholder consultation undertaken in Stage 2, thereby reducing the amount of time required to complete the rule change from around nine months to six months. Overall, the Council would have the option of reducing the rule making process from the start of the initial review to the final rule determination by at least six months, and potentially more depending on how quick the Council decision was.<sup>9</sup>

A schematic summary of the process is provided below.

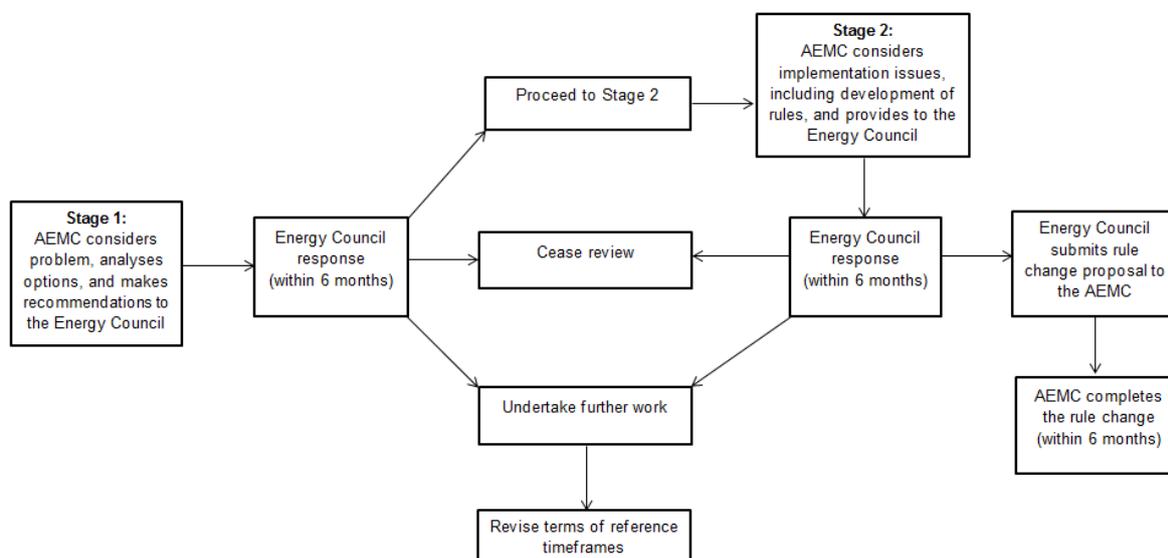
In addition to the greater speed with which the process is undertaken, benefits of this first opportunity include:

- more frequent opportunities for the Council to determine policy priorities as it would provide input between Stages 1 and 2;
- issues for review may be progressed more logically and methodically, with higher level issues being dealt with first and on their merits, with implementation issues kept separate and less likely to cloud the policy debate;
- stakeholder engagement would be clearer, more focussed and certain at each stage; and

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<sup>9</sup> The AEMC typically takes nine months to undertake a review which then typically takes the Council eight months to action. The AEMC then spends another 10 months undertaking the requested rule changes, bringing the total time to approximately 27 months. In the new approach, the AEMC's review timeline is not altered but the Council's decision making is reduced to six months and the AEMC's rule making process is also shortened to six months thereby reducing the overall time taken to 21 months.

- stakeholder consultation during a specific implementation phase would make a six month rule making process more achievable where Council has approved the policy position.



### (ii) Single step response to an AEMC review

For AEMC reviews aimed at addressing specific or contained issues, a swifter rule making process could also be achieved. In this process, we are suggesting that a single step Council response following receipt of an AEMC review final report will again allow a shorter rule making timeline.

Under this approach, the terms of reference for the review could require the AEMC to:

- address the policy issues;
- make recommendations; and
- if rule changes are included in those recommendations, set them out clearly in the AEMC's final report for the review (eg, by attaching a prepared rule change request with either draft rules or detailed draft rule specifications to the final report).

When considering the AEMC review final report, the Council could then make a decision to approve the review's recommendations and also the rule change request attached to the final report. The Council would then forward the approved rule change request to the AEMC with the meeting communiqué. Again, the AEMC would commit to a six month rule making timeline under these circumstances.

In situations where the Council does not agree with AEMC review recommendations and/or draft rules, it could either direct the AEMC to undertake further work or develop its own rule change request, within a reasonable time period.

Under this second opportunity, while the AEMC would need to do more work up front in terms of preparing the rule change requests for the Council in parallel to conducting the review, the benefits of this approach include:

- it simplifies the overall process for the Council;

- the next steps for the AEMC are clear, in terms of rule making, and it allows Senior Officials to focus on higher level policy issues rather than detail which would be addressed as part of the rule making process;
- it maintains the momentum with stakeholders;
- it has the potential to result in policy being implemented sooner for issues where clear solutions have been identified;
- it has the potential to remove the need for the AEMC to prepare a consultation paper on the rule change proposal when initiation of the rule making process and prior to making a draft rule determination; and
- it does not affect public consultation, which is highly valued by stakeholders as part of the standard AEMC rule making process.

Under this approach, as it typically takes around eight months for the Council to consider and respond to AEMC review recommendations, there is a potential time saving of up to eight months if the Council considers and approves its response to AEMC review recommendations at the same time. In terms of the AEMC, by committing to a six month rule making timeframe following receipt of a Council response, as compared to a typical rule making timeframe of around 10 months following a review, there is a potential time saving of around four months by the AEMC. Overall, this means that the post-review rule making process under this approach has the potential to be several months faster, reducing the overall timeframe from 18 months to no greater than 12 months.

### (iii) Expedited rule making process

The third opportunity, which we are already trialling within situations where the current legal provisions allow, is for an expedited rule making process (eg, used for the 'National gas bulletin board capacity outlooks' rule change (2013)).

Changes could also be made to the national energy laws to facilitate a process that is longer than the (six week) expedited rule making process, but less than the standard rule making timeframe.

Under this opportunity, we are taking the following action:

- Rule change requests can currently be processed under an expedited process (ie, within six weeks) where they are considered 'non-controversial' or 'urgent' within the meaning of the energy laws. Sometimes, the expedited process is requested by rule proponents, and at other times it is not. In either case, it is the AEMC's decision on how to proceed.
- While some rule change requests meet the test for being expedited, six weeks is not usually adequate to process the request in an appropriate manner (eg, due to a need for stakeholder consultation or complex rule drafting, even if the issue itself is clear). In cases where the test for expedition under the energy law is met, we are more actively considering use of the (six week) expedited rule making process, even when not requested by stakeholders.

- In appropriate situations, we are adopting the expedited process and extending it by two weeks (eg, by use of a section 107 notice under the NEL), so that we can subject more rule change requests to an expedited process.

(iv) Other steps

The fourth opportunity, which we are already taking, is a series of enhancements to the rule change process, which include:

- commencing rule change requests sooner, where appropriate, by undertaking less detailed analysis upfront and scoping out major issues instead (eg, used for the ‘Victorian jurisdictional derogation (smelter agreements)’ rule change (2014));
- preparing more streamlined consultation papers for rule change requests (eg, used for the ‘STTM settlement surplus and shortfall’ rule change (2014)); and
- publishing rule change requests prior to commencement, and within two weeks of their receipt after initial review, to improve transparency and provide greater consistency where the rule proponent has already published the rule change request on its website (ie, our approach to rule change requests received since late-2014).

***Question 26 — Should the AEMC be given an increased gas market reporting role, in a similar manner to its electricity price reporting?***

To date, the AEMC has prepared five annual residential electricity price trends reports. The reports provide information on possible future trends in residential electricity prices for each State and Territory across Australia. The reports are a diagnostic tool to identify the source of drivers in residential electricity prices and what parts of the supply chain require policy or regulatory attention. In the 2014 report, trends in both standing offer and market offer prices were also provided.

If the Council considers that similar information would be useful in a gas context, and that the information will be forward-looking to help inform policy, then there would appear to be good reason for the AEMC to complement its electricity pricing report with a similar gas report. A key consideration in this regard would be the availability of information to undertake the gas pricing analysis (eg, availability of contracted wholesale gas prices and gas reserves), which could be harder to obtain than for electricity.

## Section 4 — Australian Energy Market Operator

**Question 28 — To what extent does AEMO’s role as an independent national energy market operator and planner continue to remain relevant to delivering a more integrated, secure and cost effective national energy supply in today’s market? What is your assessment of AEMO’s leading strengths and shortcomings on delivering on those outcomes?**

There is a need for an independent market operator to operate, settle and develop supporting market procedures and business systems for the national electricity and gas markets. Through its daily engagement with market participants and industry consultative forums, AEMO is also well positioned to work constructively with these stakeholders to evolve the market procedures and business systems over time, and in a way, that supports the national energy rules and objectives. Any perceived or actual conflicts of interest between AEMO’s market operator and planner roles need to be managed appropriately (see response to Question 32).

**Question 32 — To what extent do AEMO’s different roles in the national market, including its responsibility for different gas trading hub designs but not the wider gas market, and having a combination transmission planner/procurer role only in Victoria, affect its ability to deliver better national market outcomes? Is there a case for expanding or reducing AEMO’s role in any areas?**

The AEMC considers the best approach to transmission planning is one where transmission network service providers (TNSP) are responsible for investment decisions and are exposed to financial incentives, and are subject to effective incentive based economic regulation. A model where there is a planner-procurer that is separate to the asset owner blurs accountability for investment decision making and network performance. Lack of accountability makes it difficult in practice to apportion responsibility for decisions, and outcomes of decisions with a particular party.

In most jurisdictions, the national transmission planner (NTP) provides an important check of TNSPs’ investment programs in order to ensure that an efficient, strategic and coordinated approach is taken to the long term development of the national transmission grid. In Victoria, however, there is no such independent review, as the jurisdictional planning function and NTP function are undertaken by the same entity (ie, AEMO).

Further, it is our understanding that there is no ring-fencing in place within AEMO between these functions. While the synergies between the two functions might mean that this is an efficient use of highly specialised resources, it places a great deal of reliance on AEMO’s public consultation and internal decision making processes. This is particularly the case given that the Victorian arrangements do not, by design and necessity given AEMO’s status as a company limited by guarantee, provide for any AER oversight of transmission investment decisions made by AEMO.<sup>10</sup>

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<sup>10</sup> See [www.aemc.gov.au](http://www.aemc.gov.au), Transmission Frameworks Review (2013), for a more detailed discussion of these and related issues.

***Question 35 — What should the AEMO’s role be in market development? How might its current contribution be improved? Are there ways to improve its procedure development processes? Should it be given more specific roles in supporting regulatory processes?***

In order to maintain clear accountabilities, AEMO’s market development role should clearly relate to systems and processes that deliver rule determinations. This matter is explored further in our response to Question 39.

## Section 5 — Energy market relationships and related issues

**Question 38 — How positive or negative do you perceive the communication channels between the Energy Council, AEMO, the AEMC, and the AER to be? What are the opportunities to enhance the way these institutions interact with each other?**

There are strong relationships and good strategic discussions are held between the institutions. The AEMC considers there is always room for even more effective and positive relationships, particularly in terms of having a better understanding of the AEMC and AEMO's respective roles in market development (ie, development in operations as compared to market development in policy).

The relationship between the institutions should be characterised by an open dialogue, such that the institutions discuss with each other their future work program, identify opportunities to work effectively together, and resolve differences of view about who should take work forward through effective dialogue.

As a general point, the following characteristics could help the Panel to evaluate the effectiveness of performance of roles for each of the institutions that are the subject of this review.

- clear statement of respective roles – there is a clear statement of the respective roles of each organisation in a public document and, where appropriate, legislation;
- good understanding of respective roles by each organisation and stakeholders – there is a good understanding amongst the organisations and broader stakeholders about the respective roles of each organisation, such that work/analysis is allocated to the organisation whose role and functions are best suited to fulfil the role, and stakeholders understand which organisation to engage with on particular issues;
- open dialogue between all the institutions to discuss opportunities, work programs, and who is to lead work – the relationship between the institutions is characterised by an open dialogue such that the institutions discuss with each other their future work program, identify opportunities to work effectively together, and resolve differences of view about who should take work forward through effective dialogue (there will be some limits around the sharing of information, reflecting legal obligations and confidentiality); and
- positive external stakeholder observation and perception of all institutions interacting and being effective – external stakeholders observe and perceive that the organisations interact effectively together to achieve their statutory roles.

**Question 39 — To what extent do the roles and responsibilities of the different institutions, as laid out in the AEMA, [remain] consistent with the establishing legislation?**

It is noted that under clause 5.1(a) of the AEMA, the jurisdictions agreed that the AEMC was to be responsible for rule making and energy market development at a national level, including in respect of the NER, NGR and NERR (reflected in clause 8). Whereas under clause 5.1(c) of the AEMA, the jurisdictions agreed that AEMO was to be responsible for the day-to-day operation and administration of both the power system and electricity wholesale

spot market in the NEM, the retail electricity markets, the retail and wholesale gas markets and other support activities. No market development role is assigned to AEMO under the AEMA.

Under both the NEL and the NGL, the AEMC has market development functions conferred on it. These functions are fulfilled by the provision of detailed advice to COAG, either requested by it, or initiated by the AEMC in relation to the operation and effectiveness of the rules or any matter relating to the rules.

Under the NEL and NGL, a number of AEMO's functions are also relevant to market development, particularly in relation to gas markets, where AEMO's functions extend to the conduct of market trials.

While acknowledging that both market institutions have an important energy market development role to perform under law, we consider that a clearer distinction needs to be made between the market development role in operations that is performed by AEMO, as compared to the market development role in policy that is performed by the AEMC. This distinction has not been consistently applied over time. The consequence of this can be that market participants and consumer advocates are not clear on whom to approach to discuss an issue, and may try to approach different parties on different issues.

From a framework point of view, it is clear there is going to be some overlap between the AEMC and AEMO in relation to market development. AEMO is charged with promoting the development and improving the effectiveness of the operation and administration of the electricity and gas markets. This is an appropriate role for the market operator, as the market operator will have direct experience of how certain aspects of the markets' operation may not be producing the intended outcomes, or are otherwise not working in practice. The market operator would also have considerable interface with industry participants, often on a daily basis, and so is likely to receive regular and immediate feedback on market difficulties.

Importantly, by defining this function by reference to market operations, arguably this function, viewed in isolation, is limited to addressing defects that present operationally (ie, technical and administrative matters), rather than considering market design in a 'clean sheet' sense. The nature of the issues that are considered at, for example, AEMO's industry consultative forums would support this. However, many of AEMO's other functions, such as its gas trading exchange function or its planning role, cannot, arguably, be discharged without often considering broader issues, such as the direction a market is, or should, be taking and fundamental market design issues. Therefore, the totality of AEMO's functions, as they relate to market development issues, makes any overlap with the AEMC's functions of market development more concrete and therefore its governance and accountability framework is important.

Inevitably, in both organisations discharging its functions, there is the possibility that one organisation is engaged on an issue that is also relevant to the other's market development related function. To an extent, close communications between the market institutions on their respective work programs may help to minimise the potential for duplication of work, as well as appropriate decision making. Stakeholders will also benefit from clarity about who is expected to perform different roles.

**Question 40 — Does the broad division of mandates between these institutions remain appropriate? Are there relevant international models of alternatives the Panel should be considering?**

The broad division of mandates between the market institutions is appropriate. For the purpose of minimising the potential for duplication of roles, confusion among stakeholders and wasting scarce resources, it is important to have clarity in the Council's written communications which publicise the allocation of tasks across the market institutions, so that the behaviours of the market institutions are consistent with the tasks that are allocated them. This also facilitates the assignment of clear accountabilities to the market institutions so that the Council can better manage the implementation of its energy market reform agenda.

**Question 41 — What are the opportunities to enhance the way these institutions interact with stakeholders and the broader community?**

In recent years, the AEMC has consciously and deliberately focussed its resources toward facilitating greater interactions with stakeholders and the broader community so that opportunities for mutually beneficial exchanges of information are not missed.

For example, the standard AEMC communication materials that we publish for each rule that we make includes the:

- final rule determination, which is the document that explains the AEMC's reasons for making the rule and how it contributes to the long term interests of consumers;
- information note, which is generally a two-page summary of the keys aspects of the final rule determination, focussing on what the rule means for consumers;
- webtext, which updates the dedicated project page for the rule change on the AEMC's website, such as adding a summary of the final rule determination to previous key milestones for the rule change; and
- news announcement, which notifies all subscribing AEMC stakeholders by email of the final rule determination and includes a link to the project page for the rule change.

Our interaction with stakeholders includes a commitment to clear and easy to interpret communication materials, especially for technically complex rule changes and reviews (eg, by simplifying complex matters into specially created info-graphics, or by providing companion Q&A notes). We also facilitate specific reference groups and workshops to engage stakeholders on key issues and inform our work (eg, workshops, forums and meetings for our 'Expanding competition in metering and related services' rule change, Retail competition reviews, East coast wholesale gas market and pipeline frameworks review, and Optional firm access review).

Our interaction with the broader community extends to participation in regional and national media interviews to explain the reasons for our decisions and recommendations (eg, communicating the findings from our retail competition reviews, including potential opportunities for obtaining better energy deals from retailers), how our work advances the national energy objectives, and highlighting the potential opportunities that are available to the benefit of consumers through greater engagement with energy markets (eg, by shopping around for a better deal from energy retailers).

Where opportunities have become available, we have actively engaged with the appropriate market institutions to coordinate joint participation in forums and workshops for the purpose of better informing stakeholders and our work through mutually beneficial interactions (eg, presentations from AEMC/AEMO staff at optional firm access review workshops and from AEMC/AEMO/AER staff at the Reliability Panel's Generator compliance template review workshop).

***Question 42 — What are the opportunities to improve the extent and consistency of responsibilities and roles by individual jurisdictions under these energy market governance arrangements?***

As noted under Question 4, there is potential for greater clarity between the Council's strategic objectives and supporting work program, including clear communications and progress reporting.

***Question 43 — What are the opportunities to improve integration between energy market, efficiency and sustainability agendas?***

While it is legitimate for governments to pursue a range of different policy objectives, it is important that this is done in a way that allows for different objectives to be effectively reconciled. Otherwise, pursuit of one objective may undermine achievement of other equally important objectives.

Further, development of government policies without due consideration of their likely effects on the operation of energy markets also introduces uncertainty into the AEMC's rule change process.

The AEMC makes changes to the rules in accordance with our statutory objectives, whose primary purpose is to promote the long term interests of consumers with respect to a specified set of variables. But what is efficient under one set of government policies may not be so under a different set of policies, where such policies have been developed in a way that is incompatible with the energy markets they affect. Changes to market rules may no longer be 'fit for purpose' as the policy landscape changes. This may lead to unintended and unpredictable outcomes for market participants.

The AEMC considers it important that the development and design of government policies (eg, emission reduction policies) are effectively integrated with energy markets so that they do not distort market mechanisms and signals. In this regard, it is important that the institution that is responsible for market development is involved in the development and design of the specific mechanisms and instruments used to achieve these policy objectives, to ensure they are effectively integrated in a manner that minimises the overall costs to consumers.

In the AEMC's recent submission to the consultation paper on the Emissions Reductions Fund (ERF) safeguard mechanism (2015), we noted while the level of emissions and the emissions reduction policy framework is a matter for the Government, the particular way the safeguard mechanism is designed is of interest to the AEMC to the extent that it impacts the way the electricity market operates, the effectiveness of its pricing mechanisms, incentives and risk allocation. In our submission, we noted that the linkages between energy and

emissions reduction policies are such that the safeguard mechanism needs to be designed with a view to achieving both sets of policy objectives. Without an integrated approach, neither the National Electricity Objective nor the Commonwealth Government's emissions reduction objectives are likely to be achieved.

***Question 44 — What are the opportunities to improve the governance of energy financial markets? Would a NEM Resilience Council be useful in any future governance arrangements in the NEM? What role, if any, should ASIC play in regulating electricity companies who hold financial services licenses to allow them to trade in electricity derivatives?***

To assist government decision making, the AEMC recommended in its final report on the NEM Financial Market Resilience review (2015) that relevant market regulatory bodies provide advice in a coordinated way using their existing powers through a 'NEM Resilience Council' comprising the AEMC, AER, AEMO and Australian Securities and Investments Commission (ASIC).

These bodies would help to provide the Chair of the Energy Council with the necessary expertise and information to develop an appropriate response to a failure by a systemically important market participant (or 'SIMP') which takes into account the potential implications on market participants, consumers, and the operation and structure of the market more broadly, as well as the NEM's financial stability.

In its final report, the AEMC also considered that the case for implementing the proposed reforms relating to 'over the counter' (OTC) derivatives developed by the Group of 20 (G20) countries for electricity participants had not yet been made when considered against the National Electricity Objective. The G20 trade reporting obligations are a means to increase transparency about a sub-section of the overall electricity derivative markets, namely OTC market activity.

***Question 45 — What are the opportunities to improve consumer engagement in energy market governance, particularly given the recent creation of ECA by the Energy Council?***

The success of the AEMC's work depends on active stakeholder engagement. We appreciate and value the insights and perspectives advocated by different stakeholder groups in response to our work. Small customers, in particular, are under-represented in the input provided to our work by the stakeholder community.

The creation of Energy Consumers Australia (ECA) is an opportunity and mechanism for the market institutions and Council to obtain focused and well developed customer input to those matters that are of greatest impact to those consumers. Our consumer research from recent retail competition reviews revealed the important role of information, and how this information is communicated to consumers, in eliciting effective consumer engagement in energy markets and imparting effective competitive pressures in retailers.