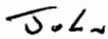


10 March 2006

Dr J Tamblyn
Chair
Australian Energy Market Commission
PO Box H166
Australia Square NSW 1215


Dear Dr Tamblyn

RE: Rule Change Request- Reform of Regional Boundaries

Thank you for the opportunity to comment on the Ministerial Council on Energy's (MCE) Rule change application to amend the process and criteria for changing a region boundary in the National Electricity Market (NEM).

While the AER supports the intent of the MCE's proposal to amend the region boundary change criteria to reflect a more economics-based approach, several aspects of the proposal require comment: the timing of the rule change; the wording of the threshold test; and an apparent inconsistency between the proposal's explanatory memorandum and the draft Rules.

Timing of the Rule change

The MCE considers a regional boundary change as an element within the broader scheme of the planning and investment framework. It is envisaged that the AEMC will only conduct a review to assess the necessity of a regional boundary change after network investment and congestion management options have been explored.

The AEMC review of congestion management is intended to consider and provide recommendations on issues affecting regional structure. Regional boundary issues are closely tied to network congestion, transmission pricing, and the abuse of market power by generators who affect constraints.

In light of this work and the MCE's view on the role of regional boundary changes within a broader planning framework, the AER considers that the timing of the Rule change reforming regional boundaries may warrant further consideration. The AER suggests that the AEMC complete its congestion management review before progressing the MCE's regional boundary reforms. This would facilitate the uniform implementation of any review recommendations.

Threshold test

The AER considers that an interpretation problem may arise in relation to the wording of the threshold test. The threshold test as set out in the draft Rule 3.5.2 (c) states:

“The AEMC must make a determination to make a region change basing its determination on whether the region change is likely to result in a material and enduring net economic benefit to all those who produce, consume and transport electricity.”

The AER considers that this could be construed as requiring every party who produces, consumes or transports electricity to gain a net economic benefit for the test to be met. This has the effect of setting a hurdle that is unlikely to ever be met. The AER appreciates that in drafting this provision, the MCE has endeavoured to take into account the wording used in the AER’s Regulatory Test which describes a market benefit as “the total benefits of an option to all those who produce, consume and transport electricity.”¹ However, the absence of the word ‘total’ before ‘net economic benefit’ in the draft Rule leaves it open to divergent interpretations.

The AER suggests that clarity may be brought to this issue by an appropriate revision to the draft Rule.

Inconsistency

The AER has identified an inconsistency between the proposal description and the actual draft Rules. A review process that is described in the proposal description is not reflected in the draft Rules. Specifically, while the proposal description provides that:

“After a region change has taken place the rule will also set out a process to review whether that change was successful (the review process)...²

the draft Rules do not include any provision for this. The AEMC may wish to address this issue as part of its Rule change considerations.

We would be pleased to discuss our views with you, particularly in relation to the timing of this work, and look forward to participating in the various stages of the review.

Yours sincerely



Steve Edwell
Chairman

¹ AER, *Compendium of Electricity Transmission Guidelines*, Clause 5 of the Regulatory Test, p 32

² MCE, *Rule Change Request- Reform of Region Boundaries*, p 6