

MCE

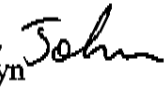
Ministerial Council on Energy

CHAIR

The Hon Ian Macfarlane MP
Minister for Industry, Tourism and Resources
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Dr John Tamblyn
Chairman
Australian Energy Market Commission
PO Box H166
AUSTRALIA SQUARE NSW 1215

3 - JUL 2007

Dear Dr Tamblyn 

Thank you for your letter of 9 May 2007 to the Chair of the Ministerial Council on Energy (MCE) Standing Committee of Officials setting out the Australian Energy Market Commission's (AEMC) proposed work program to respond to the decision of the Council of Australian Governments (COAG) that a National Transmission Planner be established as part of enhanced national transmission planning and regulation arrangements.

As you would be aware, on 13 April 2007 COAG asked the MCE to request the AEMC to develop a detailed implementation plan for the national transmission planning function, as specified in the COAG decision. This includes changes to the transmission planning arrangements, regulatory arrangements, and the form and application of the current Regulatory Test. COAG also asked the MCE to have the AEMC undertake a review of transmission network reliability standards, with a view to developing a consistent national framework for network security and reliability.

Task

Pursuant to Section 41 of the National Electricity Law, the MCE directs the AEMC to:

- a. Conduct a review into the development of a detailed implementation plan for the national electricity transmission planning function, including the most appropriate legislative amendments and Rule-changes to implement COAG's response to ERIG's Electricity Transmission Planning and Regulation recommendations (Heading 3 in **Attachment A**). The AEMC's advice must be consistent with COAG's response.
- b. Conduct a review into electricity transmission network reliability standards, with a view to developing a consistent national framework for network security and reliability.

In conducting the reviews, the AEMC should address COAG's decisions on electricity transmission planning and regulation in full. Given the relationship between the transmission planning regime and market development, investment and locational decisions, the AEMC should also take into account other relevant reviews, including:

- The Congestion Management Review; and
- The Comprehensive Reliability Review.

Consultation

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The review should also involve the AEMC:

- Consulting on a regular basis with jurisdictional representatives and the MCE Standing Committee of Officials; and
- Consulting and engaging with stakeholders under the AEMC review consultation procedures.
 - To assist in the development of the national transmission planning function and the national framework for electricity transmission reliability standards, the AEMC consultation process should include engagement with industry participants, experts and special interest groups and organisations such as the Australian Energy Regulator, the National Electricity Market Management Company, VENCORP, the Electricity Supply Industry Planning Council and Transmission Network Operators. The AEMC should also liaise with the National Market Operator Working Group.

Timing

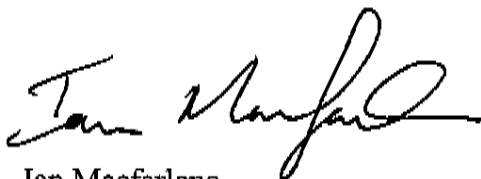
The MCE requires the AEMC to seek formal stakeholder response and consultation as follows:

- Release a Scoping Paper covering the National Transmission Planning Function and the National Framework for Electricity Transmission Reliability Standards by 31 July 2007.
- Release an Issues Paper covering the National Transmission Planning Function and the National Framework for Electricity Transmission Reliability Standards by 31 October 2007.
- Hold at least one public forum, following the release of the issues paper.
- Release a Draft Report on the National Transmission Planning Function for public consideration by 28 February 2008.
- Provide a Final Report on the National Transmission Planning Function to MCE by no later than 30 June 2008.
- Release a Draft Report on the National Framework for Electricity Transmission Reliability Standards for public consideration by 31 July 2008.
- Provide a Final Report on the National Framework for Electricity Transmission Reliability Standards to MCE by no later than 30 September 2008.

Funding

As you would be aware, the Prime Minister has agreed to Commonwealth funding for this work of up to \$1.5 million. I understand that the AEMC has been in discussions with the Department of Finance and Administration to finalise costings.

Yours sincerely



Ian Macfarlane

Attachment A

Council of Australian Governments' response to the final report of the Energy Reform Implementation Group

Attachment A sets out the Council of Australian Governments' (COAG) response to the final report of the Energy Reform Implementation Group, as contained in the COAG Communiqué of 13 April 2007.

ENERGY REFORM IMPLEMENTATION GROUP – COAG RESPONSE

At its meeting on 10 February 2006, COAG agreed that, while structural reforms taken under the National Competition Policy and other COAG initiatives have significantly improved the efficiency of the energy sector, further reform is needed to ensure Australia retains secure energy markets and relatively low electricity and gas prices. To this end, COAG recommitted to the broad ranging reforms being implemented by the Ministerial Council on Energy (MCE) and established the Energy Reform Implementation Group (ERIG) to develop proposals for:

- achieving a fully national electricity transmission grid;
- measures that may be necessary to address structural issues affecting the ongoing efficiency and competitiveness of the electricity sector; and
- any measures needed to ensure transparent and effective financial markets to support energy markets.

COAG thanked the Chairman of ERIG, Mr Bill Scales AO, and the panel members, Mr Geoff Carnody, Mr David Swift and Mr Alan Rattray for their report and for their extensive consultations across industry and government.

ERIG found that Australia's energy market is respected internationally as one of the most competitive and efficient in the world. However, COAG has accepted ERIG's view that there is scope for further reform to maintain productivity improvements and better equip Australia for its future energy needs. In response to the report, COAG has agreed to a broad ranging reform agenda that will improve competition, governance, infrastructure planning and the financial markets within the energy sector to provide a stronger industrial base for Australia's future prosperity.

1. Governance

COAG affirmed its confidence in the new energy market governance arrangements created in 2004-05 and noted that the Ministerial Council on Energy (MCE) as policy-maker and legislator, the Australian Energy Market Commission (AEMC) as rule-maker and market developer, and the Australian Energy Regulator (AER) as economic regulator, are all performing well.

COAG noted that, consistent with ERIG's recommendations, the MCE has recently completed an efficiency review of the AEMC and committed a significant increase in funding and is currently progressing amendments to AEMC rule-making legislation to assist the AEMC to better manage its workload. COAG also notes that the MCE is utilising independent expert groups to assist in the energy market reform program where appropriate.

In addition, COAG has endorsed a number of ERIG's recommendations to further improve energy market governance through the following commitments:

- establishing a National Energy Market Operator (NEMO);

- ensuring the governance arrangements for the NEMO involve market participants in board appointment processes, in a manner that preserves the board's independence from any particular market participant;
- introducing a national transmission planning function; and
- strengthening its commitment to energy market reforms through a requirement for the MCE to report annually on progress in implementing energy reforms to the COAG Reform Council to ensure agreed timelines are met.

COAG considers that these new governance arrangements will provide a solid foundation for the long term development of Australia's energy market. The performance of the new energy market governance arrangements will be examined five years after their commencement.

COAG noted ERIG's advice on the significant potential benefits arising from privatisation and/or disaggregation of energy assets remaining in government ownership. COAG agreed that any decision on privatisation or disaggregation initiatives is a matter for individual governments.

2. National Energy Market Operator

COAG has agreed to establish a single industry funded NEMO, for both electricity and gas, to strengthen the national character of energy market governance. COAG has tasked the MCE with developing, in consultation with stakeholders, a detailed implementation plan by the end of 2007 for establishing the NEMO with:

- the NEMO's functions to encompass:
 - responsibility for the day to day operation and administration of the power system and electricity wholesale spot market in the National Electricity Market (NEM) (as currently performed by the National Electricity Market Management Company (NEMMCO)), and
 - the planned Gas Market Operator (GMO), as well as the new national transmission planning function; and
- consideration to staging the establishment process for the NEMO with a transitional GMO, based on consultation with stakeholders.

The creation of the NEMO recognises the convergence of regulatory frameworks for gas and electricity as well as the economies of scale and scope arising from a single interface with energy industry participants. COAG agreed with ERIG that the NEMO should include stronger stakeholder participation and responsiveness, and has asked the MCE to develop:

- a process for appointment of an independent skills-based NEMO Board with a balanced mix of industry and generalist expertise, appointed under statutory conditions by the MCE; and
- a Market Operations Panel (or panels) for electricity and gas, to advise the NEMO Board.

COAG noted the MCE's progress in considering the establishment of a national Gas Market Operator (GMO). The GMO, if established, would be expected to subsume the gas market functions of VENCORP, the Gas Market Company (GMC) and Retail Energy Market Company (REMCORP), and have responsibility for the operation of a bulletin board and short term trading market for gas. COAG agrees with ERIG that the development of the NEMO should not delay implementation of these significant gas market development initiatives.

3. Electricity Transmission Planning and Regulation

Development of a national electricity transmission grid (excluding WA and NT) has been central to energy market reform over the last decade. ERIG has made a number of recommendations to enhance national transmission planning and regulation.

COAG has agreed to establish an enhanced planning process for the national electricity transmission network to ensure a more strategic and nationally coordinated approach to

transmission network development, providing guidance to private and public investors to help optimise investment between transmission and generation across the power system.

The National Transmission Planner, located in the NEMO, will be required to develop a strategic National Transmission Network Development Plan (NTNDP) outlining the broad development of the power system, including the current and planned future capability of the national transmission network and development options. The NTNDP will be produced after wide consultation with relevant stakeholders, have a minimum outlook of ten years and be updated and released annually.

These new arrangements will be designed to provide an appropriate balance between the delivery of a coordinated and efficient national transmission grid, and local and regional reliability and planning requirements, and be flexible enough to respond to generation and load changes. They will replace the current Inter Regional Planning Committee and Annual National Transmission Statement.

The NTNDP will provide information to the market on the longer term efficient development of the power system in order to guide network investment decisions and provide signals for efficient generation investment. The NTNDP, however, will not replace localised transmission planning, bind transmission companies to specific investment decisions, override TNSP performance obligations, or constrain the timeframes for the revenue approval process of the transmission companies. Accountability for transmission investment, operation and performance will remain with the transmission network service providers.

These arrangements are intended to assist transmission companies, when undertaking planning and putting forward their revenue proposals to the AER, to demonstrate that projects are aligned with the NTNDP. In turn, the AER will have regard to the NTNDP and the advice of the National Transmission Planner when making revenue determinations. The NTNDP will not bind the AER in its consideration of the revenue requirements of the TNSPs.

The new arrangements will be informed by the congestion management scheme (under review by the AEMC) and efficient behaviour will be rewarded through the service incentive regime (under development by the AER). The merits of aligning transmission revenue determination timetables will be considered.

COAG has also agreed to a revised network planning and consultation process, replacing the current 'Regulatory Test'. The AEMC will be tasked with advising on amalgamating the Regulatory Test criteria of reliability and market benefits and broadening the latter's definition to include national market benefits. This will allow proposed transmission projects to be assessed against meeting both local reliability standards and their ability to maximise benefits to the national market. This is intended to recognise the broader national benefits which may be achievable from investment opportunities whilst encouraging and ensuring those justified solely on reliability grounds are delivered in an efficient and timely manner.

COAG further agreed that, under the new transmission planning arrangements:

- accountability for jurisdictional transmission investment, operation and performance will remain with transmission network service providers;
- where possible, the new regime must at a minimum be no slower than the present time taken to gain regulatory approval for transmission investment;
- the new regime must not reduce or adversely impact on the ability for urgent and unforeseen transmission investment to take place;

- the roles of VENCORP in Victoria and ESIPC in South Australia, in regard to those jurisdictions, need not be changed and the new arrangements will not impose inefficient restrictions requiring additional resources; and
- the commercial arrangements relating to Basslink in its capacity as a merchant interconnection should not be altered.

COAG has also committed to reviewing the effectiveness of these arrangements after five years of operation, with a view to making further improvements if necessary.

ERIG has also recommended that the AEMC Reliability Panel review jurisdictional transmission reliability standards and develop a consistent national framework. COAG agreed that this review should be progressed, but with appropriate caution noting the different physical characteristics of the network, existing regulatory treatments in balancing reliability and costs to consumers, and that these standards underpin security of supply.

In summary, COAG has asked the MCE to:

- task the AEMC, in consultation with the AER, NEMMCO and other stakeholders, to develop a detailed implementation plan for the establishment of a national transmission planning function within the NEMO, including proposed amendments to the relevant Law and Rules for decision by the MCE;
- include the following features in the direction to the AEMC:
 - development of a strategic NTNDP, with annual updates;
 - amalgamating the Regulatory Test criteria of reliability and market benefits and broadening the latter's definition to include national market benefits;
 - consideration of alignment of regulatory periods to further reinforce the national character of the planning arrangements;
 - where possible, the new regime must at a minimum be no slower than the present time taken to gain regulatory approval for transmission investment;
 - provision for urgent and unforeseen investment to be made, when required;
 - the NTNDP will not be binding on transmission companies;
 - the AER will have regard to the NTNDP when making revenue determinations (the NTNDP will not bind the AER in its consideration of the revenue requirements of TNSPs);
 - preservation of the jurisdictional roles of VENCORP and ESIPC; and
 - leaves accountability for transmission investment, operation and performance with transmission service providers.
- task the AEMC with reviewing transmission network reliability standards with a view to developing a consistent national framework for network security and reliability, for MCE decision.

8. Timeline

Reform	Date
1. Governance <ul style="list-style-type: none"> • MCE to provide annual progress reports to COAG on energy market reforms • COAG Reform Council annual report to include energy market reform 	Dec 2007
2. National Energy Market Operator <ul style="list-style-type: none"> • MCE to develop detailed implementation plan • Establish National Energy Market Operator 	Dec 2007 June 2009
3. Transmission Planning and Regulation <ul style="list-style-type: none"> • MCE to task the AEMC with development of new regime 	June 2007

<ul style="list-style-type: none"> • AEMC to advise MCE on new regime, including proposed Laws and Rules • AEMC to report on national framework for network reliability standards • Establish National Transmission Planner and revised transmission regulation within NEMO 	<p>June 2008 Sept 2008 June 2009</p>
<p>4. Energy Rules and Derogations</p> <ul style="list-style-type: none"> • MCE to review all remaining derogations • MCE to report to COAG on remaining derogations 	<p>June 2008 Dec 2008</p>
<p>5. Retail Price Regulation</p> <ul style="list-style-type: none"> • MCE to review energy CSO mechanisms 	<p>June 2008</p>
<p>6. Financial Markets</p> <ul style="list-style-type: none"> • AEMC, NEMMCO, ASX to develop options to integrate markets • AEMC, AER and NEMMCO to address network support contracts, wholesale trading and settlement residue auctions 	<p>Dec 2007 June 2008</p>
<p>7. Western Australia and Northern Territory</p> <ul style="list-style-type: none"> • WA and NT to monitor the outcome of local and national energy market developments on an ongoing basis and consider the adoption of national institutions 	<p>Ongoing</p>