

5 June 2009

Mr Kamlesh Khelawan
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

By email: submissions@aemc.gov.au

Dear Kamlesh,

AEMC Draft Rule Determination: Arrangements for Managing Risks Associated with Transmission Network Congestion (ERC0076)

Grid Australia appreciates the opportunity to comment on the above mentioned AEMC Draft Rule Determination. This response is focussed on the AEMC's *Draft National Electricity Amendment (Negative Inter-regional Settlements Residue Amounts) Rule* (Negative IRSR Amounts Rule) of 23 April 2009.

Grid Australia notes that the AEMC's Draft Rule Determination follows previous work on this matter and the Ministerial Council on Energy's endorsement of the AEMC's 2008 Congestion Management Review's key recommendations.

Grid Australia notes that the AEMC's proposed Rule aims to:

1. Improve the 'firmness' of Inter-Regional Settlements Residues (IRSR) as a hedging instrument associated with significant network congestion;
2. Reduce uncertainty for holders of IRSR units; first by stopping the current practice of netting negative settlement residues against positive settlement residues and, secondly, by funding negative settlement residues from the Transmission Network Service Provider (TNSP) in the importing region; and
3. Promote dynamic efficiency improvements in hedging instruments that infer an increase in the level of competition in the inter-regional contract market.

As proposed, the current drafting now requires:

- that the National Electricity Market Management Company (NEMMCO) recover negative settlement residues arising in respect of a trading interval from the appropriate TNSP in the importing region (clause 3.6.5(a)(4));

- that NEMMCO recover funding for any interest costs incurred in relation to unrecovered negative settlements residue amounts from the appropriate TNSP in the importing region (clause 3.6.5(a)(4A)); and
- that the Australian Energy Regulator will be responsible for determining the appropriate TNSP to be charged (clause 3.6.5(a)(4B)).

The AEMC also contends that this Draft Rule would enable NEMMCO (later AEMO) to set a new TNSP settlement cycle for recovering negative settlements residues. This would in its view ensure that NEMMCO could recover the negative settlements residues from the appropriate TNSP in advance of the normal market settlement day, thereby preventing any potential shortfalls should the TNSP be late or miss a payment.

Grid Australia is concerned that TNSPs will be exposed to additional cash flow risks as a result of the new arrangements for recovery of negative inter-regional settlements amounts. Currently, proceeds from Settlement Residue Auctions are paid to the relevant TNSP on a quarterly basis, while payments for intra-regional settlements residues (which may be either positive or negative) are settled with the relevant TNSP on a weekly basis.

At the time of setting annual transmission prices, TNSPs must therefore make forward estimates of these amounts to ensure the correct amount of total revenue recovery. Any over or under recovery is then carried forward to electricity consumers through network charges in the following financial year.

Grid Australia notes that the AEMC's Congestion Management Review Final Report (June 2008) stated that:

"These changes, coupled with an increase in the dispatch intervention threshold to manage the accumulation of negative settlement residues, will improve the value and usefulness of the IRSR unit as a mechanism for managing inter-regional basis risk, while also noting that it will increase transmission charges to customers. The net effect to customers is not known" (p166).

This unquantified impact would appear unsatisfactory to customers, TNSPs, and impacted jurisdictions alike. In earlier reviews, Grid Australia suggested that estimates be provided on the potential impacts to affected stakeholders of funding negative settlement residues. To date, no estimates or modelling of potential negative residues have been provided. The present level of risk is therefore unknown.

The requirement for this analysis is compounded by NEMMCO's proposed change in the intervention threshold from \$6,000 to \$100,000 per event. Any uncertainty over these risks will lead to volatility in transmission prices given the annual forecasting process noted above. It is therefore suggested that the potential level of weekly inter-regional negative residues should be quantified to ensure the impacts of this Rule change are more fully understood.

Again, Grid Australia is concerned that TNSPs will be exposed to additional cash flow risks as a result of the new arrangements for recovery of negative inter-regional settlements amounts. This could occur when a significant negative settlement residue outcome is greater than the TNSP's forward estimate for any given period. In these circumstances opportunities should be sought for the recovery to be spread over more than one settlement cycle, or for the negative amounts to be netted against any positive amounts through the existing payment streams identified above, as suggested previously.

Such arrangements would assist in managing short term cash flows and better allow NEMMCO and TNSPs to manage risks associated with the new arrangements. It is noted for example that TNSPs have not to date been subject to prudential management controls under the settlements process, such as the provision of bank or other guarantees. Any additional financial requirements of this nature will clearly involve additional cost and risk for the TNSP to be funded from customers, and should be minimised to the extent possible.

Grid Australia therefore requests the AEMC to adequately address this area of concern in developing its Final Rule Determination. The proposed Rule currently requires that payments be made as determined by NEMMCO. Given these risks are to be largely borne by the TNSP under the proposed process discussed above, it would appear essential that the time, interval and method of any payments made under proposed clauses 3.6.5(4)(ii) and clauses 3.6.5(4A)(ii) should be determined by NEMMCO with the agreement of, or in consultation with, the affected TNSP. This would provide scope for efficient payment arrangements to be agreed to address the risks outlined above, and ensure the implementation of the Rule on a practical basis that minimises impacts on transmission customers. Grid Australia looks forward to working with the NEMMCO (AEMO) to this end.

Grid Australia also suggests that the AEMC give consideration to potential transitional issues to accommodate the proposed changes and their commercial impacts particularly those on TNSPs' cash flows.

Grid Australia also notes that the drafting of clause 3.6.5(4A) is expressed as being subject to clauses 11.1.1 and 11.1.2. The reference to clause 11.1.2 appears to be incorrect as clause 11.1.3 is the transitional provision that relates to recovery of interest costs.

Please feel free to contact me on (08) 8404 7983 or via e-mail Korte.Rainer@electranet.com.au to discuss any of the matters raised in this submission.

Yours sincerely,



Rainer Korte
Chairman
Grid Australia Regulatory Managers Group