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The Chairman
Australian Energy Market Commission
PO Box H166 Australia Square
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Dear Dr Tamblyn,

Draft Rule Determination: Recovery of Negative Inter-Regional Settlements Residue

In the above Determination, the AEMC has proposed to accept a Rule change proposal submitted by NEMMCO (with some modifications) intended to improve the manner in which accumulated negative inter-regional settlements residue is recovered in the NEM.

The National Generators Forum (NGF) is supportive of this Rule change, and believes the proposed new method of recovering the debt via Settlements Residue Auction (SRA) proceeds represents a positive step forward, which will improve the efficiency and value of the SRA process.

In implementing the new method, the NGF believes that a number of aspects of the Rule change as set forth in the Draft Determination could be improved. These improvements would ensure that the Rule change better promotes the achievement of the NEM Objective.

1. Intra-week Recovery

The AEMC has accepted the proposal of recovering all negative residue that accumulates beyond the value of positive residue within a settlement week on a directional interconnector via the new method, but proposes to continue NEMMCO's practice of netting negative residue off positive residue within each settlement week.

Given the accepted benefits of the new recovery method, there is a strong argument that this method should be extended to cover all timeframes, not just accumulated residues exceeding this somewhat arbitrary threshold. It is noted that the level of netting off within a settlement week can potentially have significant impacts on unit holders.

Recovering intra-week negative residues on the same basis as accumulated debt would enhance the benefits of the new recovery method, and further promote the value of the SRA process. The NGF therefore believes it is essential that the practice of netting off within a settlement week is discontinued under the new method, and that all negative settlements residue should be recovered uniformly through SRA proceeds.

Subject to any implementation issues, this could be achieved simply within the scope of the current Rule change through the amendment of proposed clause 3.6.5(a)(4A).

2. Interest Payments

The AEMC has accepted the recovery of accumulated negative residue through auction proceeds, but has proposed that the associated interest cost would still be recovered through auction fees. NEMMCO has argued that this is an inherent cost of the SRA process.

On balance, it would appear to be inconsistent to accept the principle of passing the accumulated debt through auction proceeds, but not the interest cost of funding it. This interest cost has nothing to do with the operation of the auction process, but is purely a cost associated with funding the debt itself.

To extend the efficiency benefits of this Rule change, the interest cost associated with funding accumulated debt from negative settlements residues should also be recovered through auction proceeds. Again, this could be achieved by amendment of clause 3.6.5(a)(4A), to include associated interest costs.

3. Accumulated Debt

As the original proposal was silent on this point, the AEMC has determined that the existing recovery method should be used to fund accumulated debt, and that the new method would be used to fund future debt, as at the time the new Rules commence. It is also noted that the AEMC has proposed a 3-year sunset on the changes, subject to broader review.

Given the delay of up to 2 years in the recovery of accumulated debt via the existing method, it appears that the combined effect of these proposals would be to limit the new recovery method to an effective life of 12 months, if it only takes effect in its third (and possibly final) year.

It would be preferable for the accumulated debt that remains unallocated at the time of commencement to be recovered by the new method. (It is understood for example that that the bulk of the 2005/06 debt remains to be allocated for recovery under the current method.) This preferred approach would limit recovery under the existing method to around 12 months - ie the 4 forward quarters for which auction fees have already been determined - and achieve more effective transition and earlier achievement of the benefits of the new method.

4. Other Issues

On a drafting level, it would appear that the savings and transitional Rules contained in this proposal would effectively create a new Chapter 11 of the National Electricity Rules. The AEMC may wish to consider whether the existing practice of co-locating related clauses within the Rules provides a more user-friendly approach.

The NGF appreciates the opportunity to offer its detailed comments on this valuable Rule change, and trusts the changes suggested above will enhance the benefits of the proposal.

Should you wish to discuss any aspects of this submission, I can be contacted in the first instance on (02) 6243 5120 or 0400 874 484.

Yours faithfully,

John Boshier
Executive Director