

5 November 2020

Ms Merryn York
Acting Chair
Australian Energy Market Commission
Sydney South NSW 1235

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By online submission: AEMC ERC0317

Dear Ms York

Submission to AEMC Consultation Paper – Prudent discounts in an adoptive jurisdiction

The Australian Energy Market Operator (AEMO) welcomes the opportunity to provide comment on the AEMC’s consultation paper on prudent discounts in an adoptive jurisdiction.

Victoria, as the only jurisdiction to authorise AEMO to exercise several declared network functions associated with Transmission Network Service Providers (TNSPs), is the sole adoptive jurisdiction in the National Electricity Market (NEM).

The rule changes proposed by Victorian Government (the proponent) seek to address “an apparent misalignment of obligations and incentives upon the parties” negotiating a prudent discount in an adoptive jurisdiction by “removing procedural barriers to the effective operation of the discount assessment process in Victoria” and “ensuring that discount requests in Victoria are determined in the manner intended by clause 6A.26.1 of the NER”.¹

However, rather than improving consistency regarding the application of the prudent discount regime across the National Electricity Market (NEM), the proposed changes would create more onerous requirements in Victoria than currently apply in other jurisdictions. This would appear inconsistent with both the intent of the prudent discount arrangements set out in clause 6A.26.1 of the National Electricity Rules (Rules) and one of the key principles used to test promotion of the National Electricity Objective that proposed rule changes improve consistency.

AEMO considers that the current drafting of the Rules allows prudent discount applications to be assessed as intended. Notwithstanding, this does not mean that rule clarifications and improvements cannot be made, particularly regarding schedule 6A.4 requirements which modify the application of the prudent discount regime set out in rule 6A.26 to work in an adoptive jurisdiction. However, there may be more preferable amendments than those proposed that can improve the current arrangements whilst maintaining consistency.

¹ Rule change request, pp. 5&8.

AEMO would welcome the opportunity to work with the AEMC on any improvements considered necessary and support an extension of the consultation timeframe for this expedited rule change request to allow more fulsome discussion.

AEMO's response to the three issues raised by the proponent and discussed in the consultation paper is set out below.

1. Placing negotiation and associated information obligations on the DTSO

The rule change request proposes to require the relevant declared transmission system operator (DTSO) to:

- negotiate in good faith with a transmission customer who requests, or proposes to request, a discount, and
- provide the transmission customer with information that is reasonably required by that customer to make a discount request to AEMO.

Despite the prudent discount framework operating slightly differently in Victoria due to AEMO exercising declared network functions, it is important that the Victorian arrangements remain consistent with application of the framework in other jurisdictions. The framework set out in rule 6A.26 provides for an application for a prudent discount by a transmission customer to be negotiated with a single entity, being the relevant TNSP. In Victoria, AEMO operates as TNSP for the purposes of these negotiations.

Provisions to apply the framework in Victoria provide that AEMO is the only party that may grant a prudent discount, but not without the written consent of the relevant DTSO.² For this reason, the framework also requires AEMO to negotiate in good faith with both the transmission customer seeking the discount and the relevant DTSO.³

The current arrangements in Victoria do not prevent a transmission customer from requesting AEMO provide relevant information held by a DTSO in connection with a prudent discount application. Under that circumstance, AEMO and the DTSO are required to negotiate in good faith with each other, which should also capture the reasonable consideration of information requests necessary to assess a prudent discount application.

In other jurisdictions, rule 6A.26 does not require the relevant TNSP to provide the transmission customer with information that is reasonably required by that customer to make a discount request to the TNSP. An obligation on the TNSP to negotiate with the transmission customer in good faith presumes that such information requests will be considered reasonably and in good faith.

A separate obligation on the DTSO to negotiate in good faith with and provide information to the transmission customer is unnecessary and inconsistent with the application of the framework in other jurisdictions where a single counterparty, the relevant TNSP, participates in negotiations.

² Clauses S6A.4.2(k)(3)(1) and S6A.4.2(k)(3)(2)(i) of the Rules.

³ Clauses 6A.26.1(c) and S6A.4.2(k)(3)(2)(ii) of the Rules.

2. Obligations to explain any refusal to agree to a discount

The rule change request proposes to require, for any prudent discount application in an adoptive jurisdiction:

- AEMO provide reasons for any refusal to grant a discount, and
- the relevant DTSO provide reasons for any refusal to provide its consent to AEMO granting the discount.

An amendment of the Rules to require AEMO to provide reasons for not agreeing a prudent discount would create more onerous requirements in Victoria than currently apply in other jurisdictions and introduce inconsistency in the application of the prudent discount framework throughout the NEM.

Importantly, AEMO considers the current arrangements are carefully structured so as to prevent gaming and successive discount requests being made that are tailored to seek the maximum discount amount considered most likely to be agreed, based on the specific reasons provided for the refusal of the previous application.

Where a prudent discount cannot be agreed with a transmission customer, AEMO endeavours to clearly explain its position and identify the information upon which it relies as part of its commitment to negotiate in good faith. However, any explanations provided should not prejudice future negotiations.

Requiring AEMO (or the DTSO) to provide reasons for not agreeing a prudent discount would be inconsistent with the process contemplated by clause 6A.26.1 of the Rules which provides for a negotiation. The relevant TNSP is not intended to be a decision maker that provides reasons for its decision which may be subject to administrative review.

3. Conditions around AEMO's right to apply to the AER for prudent discount cost recovery

The rule change request proposes to make amendments to clarify that AEMO's right to apply to the AER for approval to recover more than 70 per cent of a discount from other transmission customers is triggered where AEMO 'proposes to agree' to a discount on a conditional basis.

AEMO considers that 'proposes to agree' in the current drafting of clause 6A.26.2(a) is unambiguous and already includes sufficient conditionality for applications to the AER for approval of a proposed prudent discount amount on a conditional basis in all NEM jurisdictions, including applications by AEMO in Victoria. Therefore, the proposed amendment to clause S6A.4.2(k)(4) is considered unnecessary.

The proponent claims that the proposed clarification is particularly needed for prudent discount arrangements in Victoria because AEMO, as a not-for-profit organisation, does not have the same economic incentive as TNSPs in other jurisdictions to grant prudent discounts or the capacity to accept the risk that the AER refuses recovery of the proposed amount.⁴

⁴ Rule change request, p. 7.

However, not unlike AEMO, TNSPs have an incentive to fully recover any foregone revenue as a result of agreeing to a prudent discount. In any case, there can be no ambiguity that AEMO must always be in a position to fully recover revenues forgone by granting a prudent discount, irrespective of whether or not the AER approves recovery of the proposed amount in full.

AEMO appreciates the AEMC's consideration of this submission. Should you wish to discuss any of the matters raised in this submission, please contact Kevin Ly, Group Manager Regulation, on (02) 9239 9160.

Yours sincerely



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