Major Energy Users Inc.

15 May 2007

Dr. John Tamblyn
Chairman
Australian Energy Market Commission
P O Box H166
Australia Square
NSW 1215

Dear Dr. Tamblyn,

MEU Views on Congestion Management

Following on from the recent MEU submission to the AEMC's Directions Paper on Congestion Management, there are two additional matters that we would like to bring to your attention.

1. CoAG communiqué

In its response to the ERIG report, on page 4 of COAG NATIONAL REFORM AGENDA, COMPETITION REFORM APRIL 2007, CoAG states:

"These new arrangements [for an enhanced planning process for the national electricity transmission network to ensure a more strategic and nationally coordinated approach to transmission network development] 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.

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).

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."

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In its response to the Directions Paper on Congestion Management, MEU observes that it had previously expressed concerns that the decision of the AEMC not to re-address the Regulatory Test (amongst other matters) was not sound, in that the costs of congestion are so intimately tied to the Regulatory Test (RT), and that this proscribed the ambit for future congestion resolution. That CoAG now requires the AEMC to extend the ambit of the RT to include a "national market benefit" criterion must, as a minimum, require the AEMC to recognise that there is a cost penalty for a generator (with a resulting impact flow on to consumers) wishing to be dispatched but prevented from doing so because of a constraint. This now opens for dispute the AEMC decision that the out turn costs of congestion between consumers and generators in a single region as being merely and exclusively a "transfer of wealth" between consumers and generators in the region and therefore must increase the ambit of the RT to include the impact of out turn costs that congestion causes on consumers and generators in other regions.

With this in mind we seek the AEMC's assurance that the congestion management review will readdress the Regulatory Test in light of the CoAG policy decision, and that consumers will be able to comment on the new proposals for the RT to meet the CoAG requirements.

2. Insurance products

In the MEU's submission on Congestion Management, we made reference to the costs of seeking protection from price spikes (>$300/MWh) in the NEM. In further research on this issue we came across an interesting article in the Age 24 May 2006, by the respected commentator Alan Kohler commenting at the time Snowy was being readied for sale:

"...yet last financial year [Snowy generated power at] 13.5% of its capacity. ... Snowy Hydro is not really a power company ... it is an insurance company. ...Snowy makes revenue in three ways: power generation (the least of the three), insurance contracts with power retailers, including guaranteed price caps and swaps, and, third, settlement residue auctions, which involve collecting on the difference between price across a particular interconnect – say between NSW and Victoria ..."

This accurately describes the operations of Snowy, which uses its assets to increase the value of its "insurance products" and to sell these products into multiple regions.

This supports the MEU view that if there is a cost to seek protection from a volatile market (such as the NEM) then the costs of this "insurance" must be considered a cost to consumers, which is exclusive of the "transfer of wealth" debate that has so far resulted in a stunted Regulatory Test, as far as consumers are concerned.

Yours sincerely

Mark Gell
Chairman