

31 May 2011

Mr John Pierce
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Australian Energy Market Commission
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By online submission

Dear Mr Pierce

Re: Directions Paper for the Transmission Frameworks Review

AEMO welcomes the opportunity to provide feedback to the Directions Paper for the Transmissions Frameworks Review (the Review).

The need for change

This Review comes at a crucial time in the evolution of Australia's energy markets.

As the domestic economy transitions towards a low carbon environment Australia will experience unprecedented growth in the scale and importance of natural gas. Use of gas for gas powered generation in the National Electricity Market (NEM) is forecast to grow by between 300% and 500% for the remainder of the decade. Therefore the reliability and security of the NEM will become increasingly dependent on natural gas supplies.

Despite the domestic gas usage growth, the majority of gas production will be exported by the end of the decade. This has the potential to affect the price of gas and, ultimately, electricity unless there are well functioning gas and electricity markets which support efficient investment and provide investment certainty.

AEMO's modelling for the NTNDP highlights the likely location of generation investment over the next two decades. Most of that investment will be occurring in locations which are currently not well supported by the network. This investment will be driven by national supply-demand needs and national policies. This in turn will add to the congestion levels already experienced in the market unless there is a national framework to address it.

More recently price increases, largely driven by network charges, are having implications on the broader Australian community and the political landscape. Consumers are asking for a better cost-service balance. These issues have been recognised in a number of reviews. For example, in Ross Garnaut's 'Transforming the electricity sector' he noted:

'The recent electricity price increases have mainly been driven by increases in the costs of transmission and distribution¹.

and

¹ Ross Garnaut, Garnaut Climate Change Review – Update 2011 Update Paper eight: Transforming the electricity sector, p2

There is a prima facie case that weaknesses in the regulatory framework have led to overinvestment in networks and unnecessarily high prices for consumers²

Similarly, the NSW Electricity and Network Prices Enquiry noted

'Customers should have the opportunity to participate in weighing up the benefits of higher levels of reliability and the related costs including the costs associated with the probability of service failures if reliability is not improved³

More recently IPART's Consumer Summary – Changes in Regulated Electricity Prices 2011

'To address the rapidly increasing network costs arising from regulatory decisions, the Australian Energy Market Commission initiate a review of the National Electricity Rules to address concerns that these rules may bias the Australian Energy Regulator's decisions in favour of higher network prices and inefficient outcomes⁴

and

'To assess the network cost increases arising from the NSW Government's changes to service standards, the NSW Government satisfy itself that the network licence standards for network reliability and security align with customers willingness to pay and take steps to ensure that future changes to standards are subject to rigorous cost benefit analysis.'⁵

These problems can be managed with the right solutions.

Further, the emergence of smarter network technology, if deployed correctly, can have a dramatic effect on the way in which the network operates and is managed. It can also drive and influence the level of investment required in generation and networks.

In light of these challenges it is imperative that the AEMC ensure that Australia has a sustainable regulatory framework that encourages the right investment in generation and transmission in the right place at the right time. This requires the AEMC to implement regulatory arrangements that are able to withstand both market and policy changes.

We do not believe that the AEMC can find that no change or even incremental change is acceptable.

A holistic framework

AEMO understands the AEMC's need to effectively manage the workload of this review complex review. However, by splitting the work into multiple workstreams there is a risk that the AEMC will find that there are insufficient problems with individual elements to warrant reform. It is important to recognise that problems in one workstream often relate to issues in other workstreams and well designed solutions in one workstream may likewise deliver benefits in others.

For example, at the time of a connection negotiation the questions of network access are always discussed. As was noted at a recent access workshop convened by the AEMC, all parties agreed that the current framework was unworkable due to the uni-lateral nature of connection negotiations. However, as the AEMC was also made aware at that workshop, the questions of access regimes also raise questions about network planning and transmission charging arrangements.

² Op cit

³ NSW Department of Premier and Cabinet, NSW Electricity Network and Prices Inquiry, p 57

⁴ IPART, Changes in regulated electricity retail prices from 1 July 2011, p 13

⁵ Ibid p 14

We therefore encourage the AEMC to ensure that it considers linking the workstreams throughout the review to ensure efficient consideration of all possibilities and options leading to a holistic solution.

Revenue Setting

AEMO is concerned about the AEMC's decision not to conduct a review of the revenue setting arrangements, instead deferring to the AER's review. The AER's review is welcome however we understand that it will focus on the implementation of the current regulatory arrangements rather than considering options for changing the framework.

As the AEMC is aware transmission development is, in most states, driven by the revenue regulation and incentive framework and not the planning framework which consists of the Regulatory Investment Test for Transmission (RIT-T) and Annual Planning Reports.

At a minimum, the AEMC should commit to include any of the AER's findings in this review and identify how these findings interact with other elements of the transmission development framework.

Victorian Connections Framework

As the AEMC has noted AEMO has initiated an investigation into the current Victorian connection arrangements. The intention of this review is to clarify and streamline a number of more detailed aspects of the Victorian connections process within the existing Rules framework. This work has been well supported by industry stakeholders and is identifying the full range of concerns of parties seeking to negotiate connections and seeking to develop solutions.

AEMO will discuss with the AEMC any framework issues identified through this process, including those raised by energy industry stakeholders, which cannot be implemented without rule changes and which may best be addressed through the frameworks review.

If you would like to discuss any aspect of this response further please feel free to contact Louis Tirpcou on 03 9609 8415 or by email at louis.tirpcou@aemo.com.au.

Yours sincerely

David Swift

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