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John Tamblyn, Chairman
Australian Energy Market Commission
Level 16, 1 Margaret Street
Sydney NSW 2000

By email: submissions@aemc.gov.au

Dear John,

| **ENFORCEMENT AND COMPLIANCE WITH THE TECHNICAL STANDARDS UNDER THE NATIONAL ELECTRICITY RULES**

Origin Energy (Origin) appreciates this opportunity to provide a submission to the above consultation.

Origin considers that an appropriate technical standards governance and regulatory framework is vital in ensuring the reliability and security of energy supply in the NEM. Forming an important component of such a framework is an enforcement and compliance regime which provides sufficient incentives for generators to comply with their performance standards. The serious adverse consequences of power system incidents as noted by the AEMC in its issues paper are acknowledged in this respect.

It is critical, however, that the performance standards that underpin such a framework themselves are clear, fair and commercially achievable: vague and excessively onerous standards will create uncertainty and deter participation and competition in the NEM. In this context, and in support of the NGF submission to this consultation, we have some reservations with regard to technical standards currently in place in the NEM. They are ambiguous in some circumstances and excessively onerous in others.

For example S5.2.5.3 of the National Electricity Rules (NER) requires *inter alia* specific performance standards with regard to generator responses to low frequency events that are beyond the physical capability of most gas turbine plant. Exposing generators to a rigorous compliance and enforcement regime for levels of performance which may be unachievable is, in our view, inappropriate. Consultation on such a compliance framework may also be considered premature when much of the content of the technical standards is under review by NEMMCO and yet to undergo a formal AEMC consultation process. For example, strict compliance obligations may be imposed for specific performance levels which, in light of a comprehensive technical standards review, are subsequently determined to be unrealistic.

Origin is therefore inclined to agree with the NGF that the current review on compliance and enforcement should perhaps be postponed until a full AEMC consultation on existing technical standards, and the changes to these standards proposed by NEMMCO, are properly finalised and agreed upon by all participants.

However, current inadequacies of the technical standards regime aside, we now briefly address some of the key questions posed in the issues paper.

1. Are there other technical standards that the Commission should consider as part of this review?

Consistent with the NGF on this matter we would like to see transmission companies themselves made subject to enforceable performance standards with regard to the broader system standards that determine the security and reliability of the transmission system. Two of the system incidents referenced in the enforcement and compliance issues paper originated in transmission element failures. Given the essential interaction between transmission and generator performance in preventing such incidents, it is essential that this interaction is appropriately reflected in the balance of accountabilities and incentives between generators and transmission companies.

2. Is the process for establishing new performance standards effective in achieving desired outcomes for the power system? Is NEMMCO's role in the process effective or does it need to be more clearly defined?

Origin has no real concerns with the process in terms of automatic and minimum standards; however, we do not consider a negotiation framework with respect to performance standards is workable given the imbalance of negotiation power between connection applicants and transmission companies. This provision in the rules is unlikely to be used very often in our view. Nevertheless, where connection at a negotiated standard is being sought it is currently a lengthy and complicated process with a lack of clear delineation in accountabilities between NEMMCO and transmission companies. Specific responsibilities and accountabilities between the two needs to be better defined in the rules.

As an additional point, the costs of negotiating performance standards are not related to the size or importance of a unit. This means that it can be very expensive for a small generator to negotiate standards, thus acting as a barrier to entry for smaller participants. We consider some form of grading of units may be appropriate here; particularly given that the role of smaller units in system incidents is much less significant compared with larger units.

3. Are performance standards for existing plant, which were defined with reference to a derogation, an accurate representation of the capability of the plant? Are there events that should trigger a review?

Origin agrees that derogations in some cases may not reflect accurate representations of the physical capability of plant. Grandfathering of performance standards should only occur for performance which matches the capability of the plant. Where derogations are in place that allow for an obligation below this we consider it is appropriate that they be reviewed, as this may constitute a competitive advantage to those generators. Derogations that vary the level of obligation with regard to performance standards between participants should only reflect differences in technological capability in meeting such standards.

However, any derogation, or amendment to derogation, should only be implemented upon full consultation with market participants and must undergo a transparent AEMC rule change process

4. Should there be a mechanism to modify a performance standards, either at the request of participant or take account of changes in the requirements on the power system?

Origin would support a mechanism which allowed for independent review, such as by the AEMC or the Reliability Panel, of performance standards on request by participants; particularly where performance standards may become less onerous due to technological improvements in transmission operation over time. However, existing participants should not bear the cost of any required increases in performance standards once these have been established in their connection agreements. Retrospective changes in obligations regarding technical standards, like any retrospective regulatory imposition, will increase perceptions of regulatory risk for market participants and thereby discourage investment.

These costs should be borne by transmission companies themselves and recovered through regulated revenues or may be better managed through network support agreements and/or transmission investment.

5. Are there any aspects of the content of the various technical standards specified in the NER that require clarification?

As discussed in our introduction, generators (and we provided a specific example ourselves) consider that many of the technical standards are ambiguous and onerous. We note that NEMMCO has undertaken its own review on this matter and has submitted amended technical standards to the AEMC for consultation. Consideration of an enforcement and compliance framework prior to final agreement on the essential content of technical standards would seem premature.

6. Is the current framework for compliance programs effective in establishing and maintaining compliance with performance standards?

The compliance framework in the national electricity rules lacks definition and clarity, particularly with regard to the scope and content of appropriate compliance programs, and how breaches should be handled.

The substance of compliance programs appears to be largely determined by NEMMCO and transmission companies, with little room for negotiation by market participants. Perhaps the AEMC is better placed to consult with market participants and ultimately decide upon compliance programs. Origin considers the substance of what constitutes an appropriate compliance program and a clear and fair compliance framework needs addressing.

7. Is it reasonable to expect a participant to meet an absolute standard of compliance when this cannot be guaranteed through compliance programs

An absolute standard is appropriate provided participants are given some leeway around the standard to reflect their level of control, unintended errors or lapses in a fast paced dynamic environment. A more liberal interpretation of what constitutes a breach of an absolute standard in this environment may be appropriate. Non-compliance should be defined as a failure to undertake appropriate remedial action upon breaching a standard, rather than, strictly, immediate breach of a standard itself. It does not appear that the technical standard provisions in the rules reflect this important distinction in many cases (see for example clause 4.15(a)(1)). More flexibility in this respect would encourage

participants to be more open and honest about their breaches and supply relevant information to NEMMCO when required.

8. Are there sufficient incentives to ensure that all breaches of performance standards are reported to NEMMCO by participants?

There may be little incentive to report such breaches, even in the current environment, where participants are subject to civil penalties of up to \$100,000. It is therefore very important in our view that performance standards are clear and penalties are consistent with the level of control generators have over their performance at various times. Penalties should reflect an appropriate balance between the degree of control and market impacts. Due to the inherent uncertainty surrounding causation in system incidents, the legal framework underpinning performance standards should focus on corrective actions taken to restore breaches, rather than strict liability with regard to breaches themselves.

9. Is the AER the appropriate body to monitor compliance? Is the AER's approach to its monitoring role appropriate? To what extent should it monitor reactively or proactively? What other approaches to the monitoring role may be cost effective.

As the AER enforces and administers the rules it is appropriate that it monitors compliance. However, at a practical level we consider NEMMCO is better placed to engage in the day to day monitoring of technical compliance, with any breaches (liberally defined of course) referred to the AER for further investigation and enforcement if necessary.

10. Should there be some form of public reporting on the outcome of the AER's monitoring role, including non-compliance instances and what action has been taken to correct those non-compliances?

Origin considers this would be desirable as it would act as an incentive for compliance while also allowing other market participants to learn from the breaches of others.

11. Does NEMMCO's role in determining the time frame to rectify the breach appropriate and does NEMMCO have sufficient guidance in making that determination?

Origin considers it appropriate that NEMMCO assesses compliance with technical standards assessed on a case by case basis depending on the particular breach in question, market impacts, what constitutes an appropriate time period and/or best endeavours with regard to rectification of breaches. However the level of discretion this implies for NEMMCO, the appropriate length of a rectification period and what constitutes reasonable endeavours should be more clearly defined in the electricity rules.

12. Is the enforcement regime, including the powers of the AER adequate for the effective enforcement of breaches of performance standards?

The recent MCE directed review of electricity legislation has created a new regulatory framework and significantly reworked administrative penalty regime. We believe these to be more than sufficient for the effective enforcement of breaches.

13. Should NEMMCO be required to inform the AER of potential non-compliance earlier than at the end of the rectification period? Should NEMMCO refer the issue to the AER in all cases, or should NEMMCO have some discretion to extend the period for compliance?

NEMMCO should only be required to inform the AER of non-compliance once participants have been given a reasonable chance to rectify the breach. NEMMCO should have the discretion to extend the rectification period where participants are engaging in their best efforts to rectify the breach.

14. Are there other matters that the NER should require to be taken into account in proceedings?

The key issue is whether participants have acted in "good faith" or with "reasonable endeavours" to address breaches and that an appropriate compliance program is in place.

15. Are there good reasons for having two investigations into power system incidents? Does this dual process assist in resolving issues by separating operational matters from enforcement matters, or does it place an inappropriate burden on participants? Do the AER and NEMMCO have appropriate power to conduct their investigations?

Origin agrees that it may be appropriate to have an operational investigation run by NEMMCO followed by an enforcement investigation providing any informational demands on participants in respect of the latter is purely supplementary to the former. Participants should not have to supply the same information twice.

The powers of the AER and NEMMCO in this respect will need to be clarified.

16. Does the threat of enforcement action by the AER act as a disincentive to provide information to NEMMCO on a co-operative basis, if it is to be shared between the two organisations?

This can be minimised if there is an appropriate separation between the information provided and a possible penalty. That is, participants will be much more willing to provide information with respect to a breach if they are given sufficient opportunity to rectify the breach and thus avoid the penalty. However, inevitably participants with inadequate compliance programs or those unwilling or unable to rectify breaches will be the least likely to submit relevant information. The AER would have the power to request such information in the enforcement limb of the investigation. Cooperation in this regard should be reflected in the severity of the penalty to provide a financial incentive to cooperate.

17. Are the penalties for breaches of performance standards adequate?

Origin considers these to be adequate. Penalties for up to \$100,000 with public shaming are more than sufficient to encourage appropriate behaviour in our view. We do not consider that \$1,000,000 penalties are appropriate for breaches of performance standards. There are simply too many contributing variables to system incidents and their follow on market impacts (including contributions from transmission companies and

NEMMCO) to reliably allocate cause to a single party breaching its performance standards. Penalties that are out of proportion to participants' level of control over a breach or contribution to system incidents will deter competition and participation in the NEM.

18. Is there a case for determining a technical standards penalty provision which better reflects the potential costs for end users of non-compliance? If so, what should the level of that penalty be?

We disagree with this proposal and refer you to the answer to 17.

19. How might an infringement notice approach be applied in ensuring compliance with technical standards? Are there other orders which may assist in ensuring compliance with technical standards?

Origin consider an infringement notice approach as currently in the NEL for other rules breaches would be worthwhile to extend to technical standards breaches; as the penalties are not excessive and provide scope for participants to avoid costly legal processes and public shaming. It appears to be a relatively low cost way to encourage appropriate behaviour.

20. Should NEMMCO be required to consider the commercial incentives or opportunities provided by its action in managing the impact on power system security of a breach of performance standards?

This may not be appropriate for an independent market operator; in particular given the complexity and subjectivity inherent and judging market outcomes. This could lead to distortions and accusations of bias on the part of NEMMCO if some participants are affected adversely and others are not. NEMMCO should focus purely on its obligations under the NEL and national electricity rules and avoid any actions which are solely or partly directed at affecting market outcomes.

21. Is clause 5.7.3(e) sufficiently clear to allow NEMMCO to use this clause to manage a power system incident?

Origin believes this provision is sufficiently clear and provides NEMMCO with the necessary powers to ensure system security.

22. What other alternatives could be considered to address the issue of a participant gaining financially from a breach of performance standards?

Origin considers that any commercial advantage as a result of a performance standards breach would generally occur only by chance; with the opposite the more likely outcome (adverse financial consequences through lost dispatch, plant breakdown, public shaming and penalties). As a consequence we do not consider this should be something that is specifically addressed. An appropriate compliance and enforcement regime as discussed in the answers to the questions above is sufficient to encourage appropriate behaviour.



If you wish to discuss any of these matters further please do not hesitate to call Con van Kemenade on 02 8345 5278 or Andrew Milne on 08 8217 5899.

Yours Sincerely,

Michael Hayes
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