



12 August 2009

Australian Energy Market Commission  
AEMC Submissions  
PO Box A2449  
SYDNEY SOUTH 1235

Dear Dr Tamblyn,

**EMO 0001 2<sup>nd</sup> Interim Report**

Origin Energy Limited (Origin) appreciates this opportunity to provide a submission to the 2nd Interim Report (the Report) regarding the AEMC review of energy market frameworks in light of climate change policies.

In summary, we are broadly supportive of the recommendations in the Report, although on a number of important points we disagree. In particular, the proposals for managing reserve requirements are overly interventionist in our view, and we draw the attention of the AEMC to submissions provided by the ERAA, ESAA and NGF which detail concerns in this regard. We will not consider this issue further in our submission.

While we welcome the AEMC's finding that congestion is likely to increase substantially under climate change policies, the proposal to address congestion by introducing a locationally varying transmission use of system charge for generators (G-TUOS) is highly problematic. Such a charge will inevitably be complex to calculate and unstable over time and appears to disadvantage particular generation technologies. Further, as a retrospective charge it affords little opportunity for existing generators to avoid or mitigate it. Its prospects for encouraging more efficient future investment decisions are also highly questionable.

On the other hand, Origin is strongly supportive of the AEMC's network extensions for remote generation (NERG) proposal. It addresses an important gap in the current regulatory framework for encouraging transmission investment more effectively in circumstances where the normal cost-benefit regulatory test for transmission (RIT-T) does not apply. This will be of considerable importance in getting necessary new low emissions generation to market in a timely fashion under challenging climate change policy objectives.

The NERG approach is intended for supporting remote connections. However we consider the principles underpinning this approach could work equally as well for harnessing transmission investment to alleviate material congestion pinch points within the network. As we discuss in some detail in this submission, we consider this may be a promising alternative to G-TUOS.

Finally, Origin is pleased that the AEMC's own analysis has borne out the concerns of retailers regarding carbon pass-through risk. The AEMC's findings in this regard reinforce those of work commissioned by retailers themselves on this critically important issue. We



draw the attention of the AEMC to the ERAA submission which includes this work as an attachment. We also highlight the link between carbon costs pass through and system security. Retailers, either directly or through contracting, cause investment in new generation. Retail tariffs need to be cost reflective in order to underpin this investment.

However, while Origin supports the AEMC's proposals for managing carbon pass-through risk, we continue to be concerned by an exclusive focus on carbon related costs in the Report. It is vital that a more holistic assessment of the transparency, consistency and effectiveness of retail pricing methodologies is undertaken. In our view, adjusting particular aspects of the pricing approach is likely to add little value if the overall approach is flawed. We consider the AEMC is, at the minimum, well placed to provide a more comprehensive assessment of retail pricing methodologies across the NEM and establish a clear set of guiding principles for reform.

In this context we conclude the submission by discussing the importance of improving jurisdictional commitment to national processes and principles inherent within the AEMA, and how the AEMA might be strengthened to achieve this important end.

If you would like to discuss any aspect of this submission please do not hesitate to contact Tim O' Grady in the first instance on 02 8345 5250.

Regards

A handwritten signature in black ink, appearing to read "CM", positioned below the "Regards" text.

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## 1. Efficient utilisation and provision of the network

Origin commends the AEMC for undertaking the necessary modelling work to provide a clearer picture of the potential materiality of congestion going forward under climate change policies. In this regard it is important that energy market frameworks promote the efficient use of and investment in the network in a manner that best contributes to reducing congestion and its associated impacts on market participants. Origin is concerned, however, that the AEMC's recommended approach, the introduction of congestion related generator transmission use of system (G-TUOS) charge, is inadequate to the task of achieving this outcome.

While we acknowledge the desirability of some locational signals in managing congestion, as we noted in our previous submissions to this consultation, we are not convinced that locational signals on their own will be sufficient to drive congestion reducing behaviour. Unfortunately, access to fuel resources for major low emissions and renewable generation technologies, in particular, is far more important than any other locational factor. As a consequence, the imposition of congestion related charges, such as G-TUOS, on new entrant generators is likely to have limited effect in changing their locational decisions and thus reducing congestion over time. Investors are more likely to refrain from entering the market and shift their funds into other sectors entirely if transmission costs become excessive.

Origin is concerned, therefore, that in relying primarily on a locationally based transmission charge in managing future congestion on the network that congestion risk will become an increasing problem under climate change policies.

Our concerns with the G-TUOS model have led us to consider at a high level some potential alternative approaches which may provide a more direct approach to reducing congestion or managing its impacts. Given the likelihood that congestion will become material in only a few areas in the network, as confirmed by the AEMC's own modelling, we still consider a selectively applied CSC-CSP model with auctioned contracts is worth further consideration. However, while we note that the AEMC provides some measured support for this model in its latest report, we also acknowledge its potential complexities of implementation and lack of wider support in the market.

An alternative option in tackling congestion which we consider to be worth further consideration is an extension of the NERG approach. This approach holds some promise for the following reasons: because it builds on the considerable work already done by the AEMC; fits in neatly within the new strategic approach to national transmission planning under AEMO; complements the new Regulatory test for Transmission (RIT-T); retains locational signals for new entrants and avoids the need for retrospective charges on existing generators. At the same time it lowers entry barriers and provides a consistent and holistic framework for linking transmission investment requirements to the needs of new entrants, regardless of whether they locate remotely or within the shared network. Origin considers that because of these benefits this approach could gain widespread market support and be implemented relatively quickly.

We discuss the detailed rationale for a NERG type approach and how it might be implemented below.



### 1.1. Stronger locational signals may not reduce congestion

The AEMC contends that congestion is best dealt with through the introduction of cost reflective price signals to generation. Price/locational signals, however, are necessary but not sufficient in solving the problem given that congestion is also as a result of underlying limitations in the transmission network. Therefore, an efficient Congestion Management Regime (CMR) must address not only the issue of generators locating appropriately but also the short-comings in the transmission investment framework. Ideally there should be efficient coordination between generation and transmission, which as Daryl Biggar points out involves more than getting the price right.<sup>1</sup>

Origin notes that there are currently locational signals in the NEM as loss factors and the prospect of being ‘constrained off’ (i.e. not getting output to market) should influence generators when making their location decisions. Despite this, most stakeholders agree and the results of economic modelling indicate that congestion will be a material issue going forward. Whilst it can be argued that the incidence of congestion could be lessened by a strengthening of locational signals via cost reflective pricing, there are some other practical issues, (particularly in relation to the expanded RET) that limit the effectiveness of locational signals in alleviating congestion, as we discuss below.

### 1.2 The expanded RET

The AEMC has noted that the expanded RET (eRET) will require approximately 8000 MW of new renewable plant by 2020.<sup>2</sup> This will significantly change the pattern and location of generation in the NEM, placing enormous stress on the existing network. It is therefore important that market frameworks ensure that transmission investment keep pace with the entry of new generation, through the efficient augmentation of the network. The proposed inter-regional (IR-TUOS) is a positive step in achieving this outcome as it should encourage TNSPs to undertake investments that confer inter-regional benefits to the market. These include interconnector augmentations which should help alleviate/prevent inter-regional congestion. Despite this, there is a further need for the transmission planning regime to be enhanced to better tackle intra-regional congestion.

Particularly in the early years most of the expanded RET will be met by wind generation. Locational decisions for renewable generation such as geothermal, solar thermal and wind are somewhat different from conventional generation, as proximity to the fuel source is critically more important. This issue is recognised in Daryl Biggar’s paper where he states ‘for these types of generators the locational variation in access to energy sources may greatly exceed even the largest feasible locational differentiation in transmission charges’.<sup>3</sup> He goes on to mention that for some investments locational differentials in transmission charges will have little or no impact on location decisions, and thus little or no impact on economic efficiency.<sup>4</sup>

Naturally it could be argued that a high enough price signal could change investor behaviour whereby the development of second tier wind sites would be considered, but such projects may not be viable if the wind resource is not sufficient to justify the

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<sup>1</sup> Biggar, D (April 2009), A Framework for Analysing Transmission Policies in Light of Climate Change Policies, p 7

<sup>2</sup> AEMC 2<sup>nd</sup> Interim Report, pg 13

<sup>3</sup> Biggar, D (April 2009), A Framework for Analysing Transmission Policies in Light of Climate Change Policies, p 13

<sup>4</sup> Ibid, p 13 and see also pp-16 and 17 for further discussion on limitation of price signals



project going forward. All costs are variable for a new entrant, unlike an incumbent whose capital costs have been sunk, and thus an excessive charge in desirable locations of the network may deter new entry and undermine achievement of the RET.

Given the somewhat limited scope of renewables to choose where they locate it seems counter-productive to simply take the view that if the price signal is high enough these generators will then choose to locate in uncongested areas. The application of the G-TUOS as set out by the AEMC will significantly increase the cost of connection and act as a barrier to entry for renewables. Additionally it will punish incumbents that are located in congested zones where there are good renewable resources, since the TUOS charge will need to be reasonably high to discourage new entrants from locating there.

### **1.3 Problems with the G-TUOS model**

#### Variability of the charge

The introduction of a new complicated variable charge applying widely throughout the NEM will create further uncertainty in the market undermining investor confidence. Potential investors and the financial institutions that support them require as much certainty as possible about potential future costs and regulatory obligations.

The AEMC has stated that the G-TUOS will be reflective of the forward looking long run incremental network costs at a particular location. The calculation of such a charge will depend on forecasts of future network congestion, load growth, new entry \ exit of customers and generators, and changing patterns of network flows. All these variables are subject to considerable uncertainty rendering the calculation of the G-TUOS inevitably complex, subjective, and open to dispute.

The annual determination of the charge will further unsettle investors in generation assets, who already struggle to manage the effects of the variability in marginal loss factors. Like marginal loss factors the G-TUOS has the potential to render previously sound investment projects uneconomic. We cite the concerns of the Scottish Generators in the UK which concluded that the TUOS charges there were unstable, unpredictable and highly volatile hence creating an unstable investment environment.<sup>5</sup>

The variability of the G-TUOS is also likely to make it more difficult for generators to account for the increased cost through hedging on the contracts market.

#### Revenue neutrality

As discussed earlier in this submission it is our view that locational signals will be limited particularly as it relates to the entry of renewables under the RET. Therefore one of the major weaknesses of the G-TUOS model is that its revenue neutrality means that there is no funding available for the building out of congestion in any instances. Thus if the price signal fails to incentivise generators to locate appropriately the G-TUOS will only result in a redistribution of income amongst generators, with congestion remaining.

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<sup>5</sup> Ibid p 4



## 1.4 An alternative to G-TUOS - extending NERG approach to congestion

### The NERG approach

The AEMC notes that the desired market outcome is for energy market frameworks to promote efficient use of and investment in the network through decentralised decision-making by individual market participants. However, implicit in the NERG concept, and one of its key strengths, is the recognition that some form of pre-building in anticipation of new connections will be desirable under challenging climate change policy objectives, which will require an unprecedented level of low or zero emissions generation to connect to the network in rapid time. The requirement for a more strategic approach to transmission investment, one that is pro-active rather than reactive to generation needs is also inherent in the creation of the national transmission planner within AEMO, and its primary role of developing a strategic 20 year forward looking national transmission plan.

Nevertheless, it is important to recognise that the NERG approach is intended to be a complement to the RIT-T and not a substitute: its focus is on transmission connections which primarily benefit generators, or groups of generators, rather than transmission investment which is considered to benefit the market more widely (and is therefore justifiably paid for by consumers). The RIT-T does not generally apply to connections within the shared network because such connections serve the interest of generators, they do not form part of the shared network. In the same way any larger connection that forms an extension to the network out to remote areas is still primarily constructed to benefit a group of generators. This is reflected in the cost allocation and revenue treatment proposed for NERGs, it is generators whom ultimately still fund the NERG.

The principal focus of the NERG approach is to reduce the up front costs and risks associated with building connection assets for first movers. By removing some of the market failures associated with private investment in transmission embodied particularly in large connection assets (i.e., economies of scale, lack of access rights) it seeks to enhance private incentives for investment in transmission and generation more generally and thereby improve the scope for and timeliness of new entry. While consumers are required to defray some of the up front costs and consequently bear the risk of under-forecast new entry, the rationale for this is that they are likely to benefit through lower overall delivered energy costs brought about by transmission which is built earlier than it otherwise would and better exploits economies of scale.

### Application of NERG approach to congestion

The NERG approach was primarily developed to reduce transmission barriers for remotely located generation in circumstances where the RIT-T may not apply, or importantly, may not apply in time frames conducive to meeting climate change policy targets.

In principle, the reasons for why NERGs may not pass the RIT-T are similar to why transmission investment to remove intra-regional congestion may not pass the RIT-T: because the transmission investment in either case is considered to benefit primarily a group of generators rather than the market more broadly. In the context of intra-regional congestion, it is generally cheaper to use generation located elsewhere in the transmission network to meet demand than it is to augment the network in order to better utilise generation that might be constrained from time to time. This effect is reinforced by the fact that electricity demand is highly inelastic, meaning that any removal of intra-regional congestion via a transmission investment must deliver a large fall in the regional pool price in order to generate meaningful net market benefits



under a RIT-T. In the majority of circumstances this is unlikely to be the case and thus the investment does not pass the test. Consequently, the RIT-T, while arguably delivering transmission investment that is efficient from an overall market perspective, paradoxically works against supporting transmission investment that adequately manages congestion risk for individual market participants.

This will become increasingly problematic under climate change policies because of the significant volume of new generation expected to connect to the network and, as we have noted, the likelihood that such new entry will concentrate in areas where renewable or low emissions resources are located. Because these locations are so attractive to new entrants they are also where existing generators are likely to experience the greatest level of congestion risk and new entrants the most significant transmission related connection costs.

Fortunately, this is precisely why these locations are most conducive to the cost and revenue treatment underpinning the NERG approach, because prospects for future entry and subsequent economies of scale benefits are likely to be the most significant. The NERG approach therefore has the potential to address most of the serious congestion expected to impact market participants under climate change policies, while at the same time facilitating the substantial renewable new entry required under these policies.

The process for assessing where and when a NERG approach is applied to congestion should be the same as that which the AEMC has proposed for establishing NERGs, and includes the following key components:

- Early identification of potential areas by AEMO using congestion related information and other information at its disposal
- Following a sufficient level of interest expressed by generators (and some evidence of commitment is needed), a detailed planning process by TNSPs to identify the optimum size of transmission or connection assets in congested areas. This should include a preliminary assessment of whether the RIT-T might apply.
- Independent verification by AEMO of forecasts of potential new generation entry, given the desirability of the area and other alternatives.
- Construction of the connection and other transmission assets needed to support the connection and agreement on revenue recovery following connection applications by generators.
- A charging framework that requires connecting generators to pay only for the share of the assets they use. Customers would pay for any revenue requirement not recovered from generators if there were fewer generator connections than planned for.





### Key benefits

Finally, Origin considers the NERG approach applied to congestion holds considerable promise as an alternative to G-TUOS. We also believe it would attract wide market support because it meets a number of stakeholder concerns and requirements, which are implicit in the key benefits of the approach we summarise below:

- It addresses some of the key market failures associated with private investment in transmission capacity under climate change policies (i.e., economies of scale and associated free rider effects). By lowering transmission costs for first movers it supports new investment, particularly in areas likely to be most desirable under climate change policies.
- Because each new entrant is required to fund their proportionate share of the connection and associated deep connection costs (the latter is necessary to resolve the congestion) it maintains locational signals for new entrants.
- Importantly, it maintains or improves the level of access, or reduces the level of congestion risk, for incumbent generators in areas most likely to be affected by congestion.
- Existing generators will not have to pay a charge which they are unable to avoid or pay for new capacity which primarily benefits new competitors. Under the NERG concept the cost is shifted onto future connections.
- The charges are fixed and the costs are only borne as a consequence of the new investment. Unlike G-TUOS, therefore, generators are not paying for something which provides no benefits.
- Is a relatively simple extension of current work already done by the AEMC and is consistent with the focus of the new national transmission planning arrangements.
- It does not require complex tinkering with the RIT-T; rather it is a complement to the RIT-T and strengthens the investment frameworks ability to build out congestion where it becomes a significant.
- The extension of NERG approach to the shared network creates a holistic and consistent treatment for resolving transmission scarcity for new entrants regardless of whether they locate remotely or within the shared network
- For all the reasons above, it improves prospects for achieving climate change policy objectives in a timely fashion and at lowest cost to consumers.





## 2. Regulated retail prices

Origin notes the AEMC currently intends to recommend to the MCE that all jurisdictions retaining retail price regulation should develop a CPRS adjustment mechanism for energy and carbon related costs which:

- can be invoked as frequently as six monthly subject to a cost change threshold;
- is symmetrical to allow adjustment for increasing or decreasing costs; and
- optimally can be initiated by retailers where costs are rising.

Overall, Origin supports this recommendation. Given the concern we have had (and that the AEMC has also reflected) that meaningful forecasting of the carbon or wholesale costs to retailers under the CPRS will essentially be extremely difficult, it would seem reasonable that retailers themselves have the capacity to adjust prices to manage their risk. Providing for a six monthly adjustment also addresses the concerns Origin had about the limited flexibility of the existing jurisdictional pricing periods. (We recommend that there should be an annual review in any event.)

However, Origin believes more needs to be done, as discussed below. In particular, there is a significant gap in practice between the commitment to full pass through, and the reality of achieving this. In the end, the reality will be totally conditional on the data, the assumptions and the modelling framework that each regulator selects for their analysis.

We are concerned that if this does not occur and in the absence of some over-riding principles for assessing “cost pass through of carbon”:

- (a) we believe the recommended principles as set out by the AEMC will not sufficiently decrease the risks to retail competition and of retailer failure (Question 5b); and
- (b) the existing approaches will also not be adequate to assess the cost to retailers of the expanded RET, particularly in the context of the yet unknown interactions between RET and CPRS. Origin agrees with *Roam Consulting* in their analysis of market impacts when they say “*the interaction of the RET and the CPRS is poorly understood, and requires substantial further investigation*”<sup>6</sup> (Question 5c).

### 2.1 Understanding the ‘black box’ price setting methodologies

While the development of a retailer-initiated price adjustment is a positive step, a fundamental problem remains, which is the current jurisdictional use of ‘black box’ proprietary methodologies for developing prices. Any amendments to prices following changes to inputs and assumptions are still constrained by the limitations and relevance of the black box to the provisions of pricing outputs under a CPRS and RET constrained world.

Origin understands that the AEMC does not seek to involve itself in how jurisdictional regulators determine cost methodologies. However, Origin considers that it may be necessary for the AEMC to provide some independent assessment of the modelling framework in each jurisdiction to ensure that as a minimum, the effect of the model is to provide an appropriate pass through of CPRS. This is discussed below.

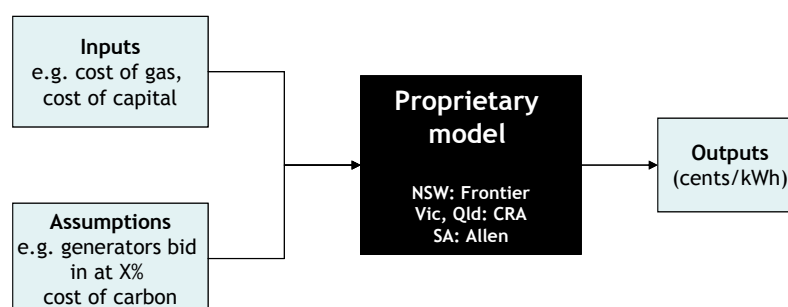
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<sup>6</sup> *Roam Consulting*, Market Impacts of CPRS and RET, 17 December 2008.

Regulators traditionally purchase modelling services from external consultants and prices are an output of these proprietary models. Currently there is no transparency in the methodologies regulators use for price setting: retailers do not know the assumptions built into the models by the various consultants, or the nature of the sensitivity analysis that is undertaken. There is also a significant range in the outputs of the different models.

What this means is that retailers do not currently know what is considered material or ‘fair’ by regulators, as the methods are essentially ‘black boxes’. Understanding various costs and assumptions is only one part of the equation - what still remains a mystery is how these come together to arrive at a price output. It should be recognised that inputs have direct and indirect effects on outputs, and how the interaction between variables is calculated is just as important as knowing inputs.

**Figure 1: The ‘black box’ approach to regulatory price setting**



Without a clear understanding of the methodology used by a regulator (via its consultant) retailers will be unable to:

- (a) know ahead of time when the cost threshold is reached from a regulator’s perspective, or
- (b) understand what the regulator may find to be reasonable in a retrospective assessment.

Retailers are thus put at a disadvantage, as they will not be able to make informed decisions about risks.

Even a best guess by a regulator and their consultant may not take decisions to where they need to be, as recently shown by events in NSW in 2008/09. Despite the opportunity for an annual review of wholesale energy costs, and the clear evidence of wholesale cost pressures, the particular model in NSW assessed that the threshold for change did not require adjustment. Origin has separately requested in its recent submission to IPART for this issue to be investigated further so that the market may have more confidence in the modelling<sup>7</sup>.

Further, it is essential that the risks associated with miss-specified models are fully understood in the context of typical retail margin allowances. Limitations in inputs,

<sup>7</sup> Origin Energy Retail Ltd: *Submission to the Independent Pricing and Regulatory Tribunal on the Issues Paper: Review of regulated retail tariffs and charges for electricity 2010-13*, August 2009.



assumptions and model specifications will have a marked effect on the actual margin achieved by retailers. In like vein, even robust models may prove to be sensitive to a range of “reasonable assumptions”.

For example, a standard regulated retail margin allowance of 5% return on sales will result in an allowed margin of around \$7/MWh for an average customer with an annual bill of \$1000. If the range of statistical and/or specification error in the modelled outputs<sup>8</sup> exceeds \$7/MWh, retailers’ margins are lost. This is a big ask of any model, let alone one that is built upon guesses about as yet unknown and untested environment. Frontier Economics have for instance demonstrated a range in feasible assumptions about model inputs that lead to a range of feasible wholesale cost outputs well in excess of the average margin allowed.<sup>9</sup>

Overall, there has been nothing demonstrated to date that improves Origin's understanding of how inputs are linked to outputs in any of the proprietary models used by regulators. This is complex enough with ‘business as usual’ price setting, with relative stable and predictable wholesale markets. The relevance and robustness of the models within the CPRS environment the situation is even more uncertain. If we then overlay people’s expectations around eRET, the complexity of the situation becomes close to unmanageable. In this respect, Origin highlights the multiple perspectives taken on generator behaviour, carbon price, and consumer response by different modellers, leading to very different views on the likely impact on retail energy costs.

There is therefore, the potential for there to be a significant difference between a jurisdiction’s genuine commitment to pass-through CPRS and eRET costs, and having the actual modelling capacity to do this, when there is no one “right” set of inputs and assumptions. Efficient and meaningful pass-through *at the least* requires transparency and consistency in modelling so that retailers are clear about how to understand and manage their risks.

As noted below, Origin strongly recommends that the AEMC promotes transparency in price setting, including robust scenario testing around assumptions and inputs at the time the framework in any jurisdiction is being established. The current situation of ‘black box’ calculations, with unknown assumptions and sensitivity analyses, and inconsistency across jurisdictions, is not going to support the AEMC’s proposed model.

## 2.2 Costs to be reviewed

While we believe that limiting reviews to carbon-related costs should reduce the administrative burden on all concerned, we are concerned that this might be too narrow a focus. Retail operating costs must also be able to be reopened because the potential for significant (but currently unquantifiable) changes in retail costs are high with CPRS, energy efficiency costs and interval metering (when that occurs). The impact of demand on pricing should also be addressed, such as energy efficiency programmes and renewables.

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<sup>8</sup> Due to either modelling specifications, or variations in inputs and assumptions

<sup>9</sup> Frontier Economics, *Impacts of climate change policies on electricity retailers*, May 2009. See for instance, pp 11-14.



### 2.3. Establishing materiality

While Origin strongly supports the AEMC's proposal (with the concerns noted above) we would also like to see some clarification about the means of calculating the threshold, and the likelihood for jurisdictional variation in this calculation.

The important thing is that the threshold is not too high. There is little point having the flexibility to adjust prices if the threshold for change is too high or not based on a reasonable perspective that is agreed by the industry. The effects will be worse if the methodology and threshold are then set in place for a long period of time.

Origin notes too, that if the energy cost forecast model is built around a Long Run Marginal Cost (LRMC) model, it is far less likely to be responsive to the very real changes in a retailer's actual wholesale energy purchase costs. In this event, the threshold may need to be lower still.

As noted below, we suggest that (a) the AEMC sets a threshold calculation methodology, and (b) the threshold calculation itself is reviewed by the AEMC after 12 months.

### 2.4 The AEMC's process and the AEMA: Origin recommendations

In previous submissions to the AEMC and other bodies Origin has stated a concern about the commitment of the jurisdictions to the Australian Energy Market Agreement (AEMA). The recent decision of the South Australian government to commit to a further period of price regulation despite the AEMC finding retail competition to be effective is an example of where commitment to the principles of the AEMA has been outweighed by jurisdictional concerns. Further, Origin notes that the two most recent jurisdictional terms of reference for the next regulatory period, while establishing objectives of cost reflectivity and encouraging competition, do not mention the final objective of price deregulation, although this is explicit in the AEMA.

The National Energy Consumer Framework (NECF) seems set to also be interpreted broadly by jurisdictions, with jurisdictions having discretion over the timing and the details of which elements of the 'national' approach to adopt. This is not reasonable and in Origin's view unnecessary given the considerable consultation and negotiation that has been conducted with all stakeholders. Origin is most concerned that such a level of discretion and what appears to be limited accountability will undermine the very benefits that the framework seeks to capture. Without a planned implementation rollout the NECF becomes just another set of compliance obligations, in addition to the jurisdiction's own rules. This will increase the regulatory burden rather than reduce it.

While we acknowledge the AEMC's lack of explicit authority to act to uphold the AEMA or require the jurisdictions to take particular actions, Origin seeks the support of the AEMC in any way possible to further jurisdictional commitment to national policy and regulation. This also means doing whatever necessary to secure jurisdictional support for the AEMC's recommendations on the CPRS and enhanced RET adjustment process.

The only practical means of improving jurisdictional commitment to national processes and principles would seem to be to improve the AEMA in both its content and power to negatively impact jurisdictions that do not adhere to the agreement. This has also been suggested by the Productivity Commission in a current consultation about regulatory costs, where in its recent Draft Paper *Review of the Regulatory Burden Economic and Social Infrastructure Services*, the Productivity Commission has found that the AEMA



should be amended to ensure stronger commitments to competition reviews undertaken by the AEMC. In our submission to the Productivity Commission on this issue (a process concurrent with this AEMC consultation) Origin also proposes additional amendments to the AEMA, as follows:

- Where jurisdictions decide to maintain retail price regulation, this is done with a clear and explicit commitment to the objectives of supporting retail competition in the regulatory period, with the goal of achieving retail price deregulation at the end of the period.
- Jurisdictions that do not move to end retail price regulation following a finding by the AEMC that competition is effective must provide:
  - a transparent rationale for their decision, using evidence to identify where competition is inadequate;
  - proposed steps to be taken by the jurisdictional government to address remaining limitations in the competitive environment;
  - a date within the next twelve months by which to report on progress in addressing limitations in the competitive environment as identified, with new measures proposed, if required; and
  - a date within the next twelve months by which time a new decision on removing price regulation will have been taken.
- Provision should be made for a portion of Federal funds to participating states to be dependent on the achievement of the goal of removing retail price regulation where competition has been proven to be effective.

Origin notes that the AEMA has been amended to specify that, where retail prices are regulated, energy costs associated with the CPRS and the RET shall be passed through to end-use consumers. COAG signed the revised AEMA at its meeting in Darwin on 2 July 2009.

For the purposes of establishing clear commitment to the AEMC's suggested regulatory principles for passing through costs from the CPRS, we suggest here that the AEMA should also be amended to provide explicitly for the following:

- The adjustment mechanism for energy and carbon related costs:
  - can be invoked as frequently as six monthly subject to a cost change threshold, and subject to review after twelve months in any event;
  - is symmetrical to allow adjustment for increasing or decreasing carbon costs and other specified operating costs; and
  - can be initiated by retailers where costs are rising.
- Jurisdictions' commitment to establishing a transparent process for price setting, including consultation with the industry on price methodologies, assumptions and sensitivity analysis.
- Jurisdictions are required to use a particular methodology for the cost change threshold (as noted above, this will require further consultation on approach).
- Provision for changes to the cost change threshold approach based on AEMC analysis of the issues after twelve months.



It is useful to note that at the COAG meeting of 30 April 2009, the MCE was tasked with providing a report by the end of 2009 on expected electricity price rises over the next three years, identifying the major components of those price rises. It is concerning, however, that at least two jurisdictions will have potentially made substantial commitments to the framework and the assumptions that they will be using for their next 3 year pricing periods through to at least 2012-13 and which cover the introduction of the CPRS.

Origin is therefore very keen to understand the process of developing this work, and hope the AEMC's findings through this consultation will be carefully and fully considered by jurisdictional regulators over the next few months.