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Dear John

REFORM OF THE REGULATORY TEST PRINCIPLES

Macquarie Generation appreciates the opportunity to comment on the MCE's proposal to establish regulatory test principles in the NEM Rules.

The Corporation does not consider that there is any case to substantially alter the existing regulatory test. As recognised by the MCE in its proposal, the ACCC made a number of major improvements to the test in August 2004, including provision for competition benefits in the application of the test.

Macquarie Generation appreciates that the purpose of the MCE proposal is to provide guidance to regulators as to the policy intent of the test. One of the Corporation's concerns is that a statement involving multiple principles can create problems with interpretation, for example in deciding how much weight to give individual principles.

The MCE faced a similar quandary when redrafting the National Electricity Law and converting the previous Code into statutory Rules. The MCE decided ultimately to establish a single, overarching market objective. Much thought and effort went into the drafting of the objective and the Corporation endorsed the final version.

Macquarie Generation favours the inclusion of the current regulatory test in the NEM Rules as proposed by the "Group"¹ in its response to the MCE's Rule change proposal. Any future change to the regulatory test would then be subject to an AEMC assessment against the NEM objective.

This model offers a number of advantages over the MCE proposal:

- the AEMC would become responsible for considering amendments to the regulatory test and the AER would retain responsibility for reviewing the application of the test by transmission service providers. This approach is consistent with the concept of separating rule making from economic regulation, which was the main reason for creating the two regulatory bodies;
- recent changes to the National Electricity Law have established robust Rule change processes and consultative arrangements that the AEMC is obliged to follow. The Corporation considers that these AEMC processes have worked well to date. The Group's proposal therefore avoids the need to develop separate processes for the AER;

¹ TRUenergy, NRG Flinders, International Power, Loy Yang Marketing Management CO and AGL, *Submission to the AEMC, Reform of the Regulatory Test Principles, Section 2*, February 2006.

- the AER would still have an important role in developing guidelines setting out the detailed methodology for applying the test.

Section 8 of the National Electricity Law allows the Ministerial Council on Energy to issue a statement of policy principles on matters relevant to the exercise of the AEMC's functions. The MCE must be satisfied that policy principles are consistent with the NEM objective. Macquarie Generation suggests that this may be a more appropriate avenue through which the MCE could provide policy guidance, possibly in response to proposals to significantly amend the test.

Principle 7 in the MCE's Rule change proposal states that the regulatory test must be consistent with the basis of asset valuation determined by the AER under clause 6.2.3, *Principles for Regulation of Transmission Aggregate Revenue*, to ensure internal consistency within the Rules. The Corporation agrees that the regulatory test should provide for this consistency and also reflect the proposed changes to the Rules governing transmission revenue regulation.² These draft changes allow for actual costs of a project to be included in the asset base provided they are prudent and efficient, rather than estimates based on information available at the time the project was commissioned.

Thank you for the opportunity to comment.

Yours sincerely



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² Australian Energy Market Commission, Draft National Electricity Amendment (Economic Regulation of Transmission Services) Rule 2006, February 2006.