



Australian Energy Market Commission

## CONSULTATION PAPER

# National Electricity Amendment (Governance Arrangements and Implementation of the Reliability Standard and Settings) Rule 2014

**Rule Proponent(s)**  
COAG Energy Council

25 September 2014  
For and on behalf of the Australian Energy Market Commission

RULE  
CHANGE

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## **About the AEMC**

The AEMC reports to the Council of Australian Governments (COAG) through the COAG Energy Council. We have two functions. We make and amend the national electricity, gas and energy retail rules and conduct independent reviews for the COAG Energy Council.

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# 1 Introduction

On 9 May 2013, the COAG Energy Council (the proponent) submitted a rule change request to the Australian Energy Market Commission (AEMC or Commission) in relation to the governance arrangements and implementation of the reliability standard and settings.

This consultation paper has been prepared to facilitate public consultation on the rule change proposal and to seek stakeholder submissions on the rule change request.

The rule change request seeks to amend the governance arrangements for determining and setting the reliability standard and reliability settings, including how the reliability standard is implemented by the Australian Energy Market Operator (AEMO).

This paper:

- sets out a summary of, and background to, the rule change request;
- identifies a number of questions and issues to facilitate consultation on this rule change request; and
- outlines the process for making submissions.

Submissions to the consultation paper are due by 23 October 2014.

## 2 Background

This section outlines the background to and current arrangements for determining the reliability standard and reliability settings, and arrangements for implementing the reliability standard. First, we provide a summary of the roles and responsibilities of the AEMC, the Reliability Panel (Panel), and AEMO. Each entity would be affected under the proposed rule and it is useful to provide context here about their current roles and responsibilities when considering the governance changes proposed in the rule change request (section 2.1).

Second, we briefly detail the role of the reliability standard and the reliability settings in the National Electricity Market (NEM), followed by the processes under which they are currently set (sections 2.2 to 2.4).

Finally, we provide a summary of the AEMC's Review of the Effectiveness of NEM Security and Reliability Arrangements in light of Extreme Weather Events from 2010. Part of the rule change request is based on recommendations made in this review (section 2.5).

### 2.1 Institutions

#### *AEMC*

The AEMC makes rules under the National Electricity Law (NEL), the National Gas Law (NGL) and the National Energy Retail Law (NERL). These rules impact on how companies can operate and participate in the competitive generation and retail sectors. They also govern the economic regulation of electricity transmission, distribution network services and gas pipelines.

Importantly, the AEMC may not initiate rule change requests other than where the proposal is to correct minor errors or is non-material.

Instead, the role of the AEMC is to manage the rule change process and to consult on and decide upon rule change requests made by others in accordance with processes and tests set out in the relevant law.

The AEMC also provides governments with advice on improvements to regulatory and market arrangements in accordance with terms of reference from the nation's energy ministers. The AEMC may also initiate its own reviews.

Membership of the AEMC consists of 3 Commissioners appointed by the Governor of South Australia on the recommendation of the relevant Minister, of whom:

- one, who will be appointed to be the Chairperson, will be a person nominated for such appointment by the MCE (States and Territories); and
- one will be a further person nominated by the MCE (States and Territories); and

- one will be a person nominated by the Minister of the Commonwealth who is a member of the MCE.

### *Reliability Panel*

The Panel was established by the AEMC under the NEL.<sup>1</sup> The role of the Panel is:

- to monitor, review and report on the safety, security and reliability of the national electricity system, in accordance with the National Electricity Rules (NER);
- at the request of the AEMC, to provide advice in relation to the safety, security and reliability of the national electricity system; and
- to manage and execute any other functions or powers conferred on it under the NEL and the NER.

The Panel is responsible for developing and publishing power system standards and guidelines to assist AEMO to perform its power system security and reliability functions.<sup>2</sup>

Membership of the Panel consists of:<sup>3</sup>

- a Commissioner of the AEMC appointed to act as Chairperson of the Panel;
- the Chief Executive Officer of AEMO or its delegate; and
- at least five but not more than eight other persons appointed by the AEMC for a period of up to three years, representing industry and consumers.<sup>4</sup>

### *AEMO*

AEMO was established to operate the national electricity market (NEM) and gas markets. Created by the Council of Australian Governments (COAG) and developed under the guidance of the former Ministerial Council on Energy (MCE) (now COAG Energy Council), AEMO is responsible for electricity and gas market functions, NEM system operations, management of Victoria's gas transmission network and national transmission planning.

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1 NEL, s. 38.

2 This includes the power system security and reliability standards; system restart standards; performance standards; plant standards; principles and guidelines for maintaining power system security; reliability and emergency reserve trader (RERT) guidelines; system operating incidents guidelines; publication of AEMO report to the Panel on ESOO demand forecasts; and development and publication of template for generator compliance programs.

3 See cl. 8.8.2 of the NER.

4 These persons must include a person representing each of the following: generators; market customers; transmission network service providers; distribution network service providers; the interests of end use customers for electricity.

AEMO's functions are prescribed in the NEL while procedures and processes for market operations, power system security, network connection and access, pricing for network services in the NEM and national transmission planning are prescribed in the relevant rules.

AEMO operates on a cost recovery basis as a corporate entity limited by guarantee. Its membership structure is split between government and industry, 60 and 40 per cent respectively. Government members include the Queensland, New South Wales, Victorian, South Australian and Tasmanian state governments, the Commonwealth and the Australian Capital Territory.

## **2.2 The reliability standard and reliability settings explained**

### *Reliability Standard*

The reliability standard is a measure of the adequacy of the electricity generating systems and networks to meet the demand of consumers. Setting the reliability standard involves balancing the value that consumers place on the supply of reliable electricity with the costs involved in delivering this level of reliability.

The reliability standard is used to evaluate whether sufficient investment in generator capacity is occurring to meet changes in consumer demand. As such, the reliability standard applies primarily to generation, but also includes inter-regional transmission.

Operationally, the level of the reliability standard specifies the maximum unserved energy (USE) acceptable as a percentage of annual demand, or the maximum amount of electricity expected to be at risk of not being supplied to consumers, in a financial year. The level is currently set at 0.002% USE per annum, which equates to the interruption of supply to every consumer in a region for approximately 10 minutes each year. This has remained unchanged since established by the Reliability Panel (Panel) in 1998.<sup>5</sup>

### *Reliability Settings*

The main function of the reliability settings is to signal the need for generation capacity and demand-side response to deliver the reliability standard. The reliability settings also provide a mechanism to limit financial risk for market participants by imposing caps and floors on prices.

The settings include a market price cap, a market floor price, a cumulative price threshold, an administered price cap, and an administered floor price. Table 2.1 summarises the objectives of each reliability setting, indicates their level and the relevant decision-maker.

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<sup>5</sup> See the 2014 Reliability Standard and Settings Review.

**Table 2.1 Summary of the currently reliability framework**

Parameter	Objective	Level	Decision-maker
Reliability standard	Indicates to the market the target level of supply and demand adequacy.	USE < 0.002% annual energy consumption of region	Reliability Panel
Market price cap	The key reliability setting. Incentivises sufficient generation capacity and demand-side response to deliver the reliability standard.	\$13,500/MWh (2014-15); CPI indexed each financial year	AEMC (rule change process)
Market floor price	The lowest allowable limit for the spot price. Aims to provide an appropriate price signal for the spot market to clear at times of very low demand and excess generation in a region by incentivising generators to offload generation when it is efficient to do so. It is generally considered unrelated to investment signals.	-\$1,000/MWh	AEMC (rule change process)
Cumulative price threshold	An explicit risk management mechanism designed to limit participants' exposure to protracted levels of high prices in the spot market.	\$201,900 (2014-15); CPI indexed each financial year	AEMC (rule change process)
Administered price cap	Designed to reduce the financial exposure of market participants during an extreme market event, while maintaining incentives for market participants to supply electricity.	\$300/MWh	AEMC (via schedule to the NER)
Administered floor price	A price floor to apply to a regional reference price <sup>6</sup> , with the level of the price floor being the negative of the value of the administered price cap.	-\$300/MWh	Rules-based

### 2.3 Current arrangements for determining the reliability standard and reliability settings

This section outlines the current governance arrangements and determination processes of the reliability standard and reliability settings.

#### *Reliability Standard and Reliability Settings Review*

Under the current arrangements, the Panel is responsible for setting the reliability standard as part of its requirement to undertake and publish a four-yearly review of

<sup>6</sup> The regional reference price is the price at which the spot market is settled in each region.

the reliability standard and reliability settings.<sup>7</sup> This review must set out the Panel's decision with respect to the level of the reliability standard and its recommendations to the AEMC in relation to the reliability settings. This review must be conducted in accordance with the rules consultation procedures.<sup>8</sup> The administered price cap and the administered floor price are not included in this review.

Although the Panel decides the level of the reliability standard as part of this four-yearly review, it may only make a recommendation and a rule change request to the AEMC in respect of any recommended changes to the reliability settings. The Panel may make such a rule change request if it finds that the current reliability settings are not set such that the reliability standard in the NEM will be met.

When conducting any review under this clause the Panel must have regard to the following factors:

- the potential impact of any proposed changes in the MPC or CPT on: spot prices; investment in the NEM; the reliability of the power system; and market participants;
- any value of customer reliability determined by AEMO which the Panel considers to be relevant; and
- any other matters the Panel considers relevant.

The Panel's review of reliability settings must set out all relevant market conditions and circumstances on which its recommendation is based. The Panel may only recommend a level of the MPC or CPT which the Panel considers will:

- allow the reliability standard to be satisfied without use of AEMO's powers to intervene under NER 3.20.7(a) and 4.8.9(a) (see discussion in section 2.4); and
- in conjunction with other provisions of the NER, not create risks which threaten the overall integrity of the market.

Further, if the Panel is of the view that a decrease in either the MPC or the CPT may mean the reliability standard is not maintained, the Panel may only recommend such a decrease where it has considered any alternative arrangements necessary to maintain the reliability standard.

The Panel may only recommend a market floor price which the Panel considers will allow the market to clear in most circumstances and not create substantial risks which threaten the overall stability and integrity of the market.

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<sup>7</sup> See NER 3.9.3A.

<sup>8</sup> *ibid.*

## 2.4 Current arrangements for implementing the reliability standard

There are few NER-based requirements as to the methodology AEMO must use to implement the reliability standard. Under the current approach, AEMO implements the reliability standard through short-term and medium-term projected assessments of system adequacy (PASA) to set minimum reserve levels (MRL) for each jurisdiction.<sup>9</sup> MRLs are the reserve margins that AEMO calculates are required to meet the reliability standard.

The proponent indicates that AEMO has interpreted these requirements by determining MRLs in consultation with industry stakeholders and the Panel.<sup>10</sup>

PASA is a program of information collection, analysis, and disclosure of medium-term and short-term power system security and reliability of supply prospects. The purpose of providing these assessments is to enable Registered Participants to be properly informed and able to make decisions about supply, demand and outages of transmission networks in respect of periods up to 2 years in advance.

If a shortfall of reserves is forecast, AEMO has the power to procure additional generation reserves under clauses 3.20.7(a) and 4.8.9(a) of the NER. This requires AEMO to negotiate and enter into contracts with reserve providers. These arrangements are known as the Reliability and Emergency Reserve Trader (RERT) mechanism. They provide a safety net in the event that the NEM does not deliver sufficient reserves to meet the reliability standard.<sup>11</sup>

## 2.5 Extreme Weather Review

This rule change request arises primarily out of the AEMC's 2010 Review of the Effectiveness of NEM Security and Reliability Arrangements in light of Extreme Weather Events (Extreme Weather Review).<sup>12</sup> The Extreme Weather Review concluded there were areas in the governance framework of the reliability standard and settings that could be improved to maintain consumer expectations for the quality of electricity supply in a future in which the frequency/severity of extreme weather events could increase.

This Review recommended that the existing governance arrangements be amended such that:<sup>13</sup>

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<sup>9</sup> See NER 3.7.

<sup>10</sup> Rule change request, 9 May 2013, p8.

<sup>11</sup> The RERT provisions in the NER expire on 30 June 2016. The RERT provisions have been reviewed by the Reliability Panel on a number of occasions, and also considered by the AEMC through the rule change process.

<sup>12</sup> This report is available on our website, [www.aemc.gov.au](http://www.aemc.gov.au).

<sup>13</sup> AEMC, Review of the Effectiveness of NEM Security and Reliability Arrangements in light of Extreme Weather Events, 31 May 2010, p. 92.

- the AEMC make all reliability parameter decisions (that is, to review and, if need be, amend the reliability standard and settings); and
- AEMO make all reliability operational decisions (including to initiate the RERT mechanism and to review and, if need be, amend the MRLs); and
- high-level policy guidance is included in the rules, which the AEMC would need to have regard to when reviewing and, if need be, amending the reliability standard and reliability settings.<sup>14</sup>

The bases for these recommendations were:

- the current governance arrangements, with separate decision-making bodies for the reliability standard and reliability settings, may restrict the ability of the NEM to respond efficiently and in a timely manner to a possible increase in the frequency and/or severity of extreme weather events;
- maintaining consistency and allowing for a single decision-maker would reduce complexity of the existing processes and ensure that there is appropriate alignment between the reliability standard and reliability settings; and
- a lack of high level guidance in the NER for setting the reliability standard and reliability settings can lead to inefficiencies and restrictions on what information can be taken into account as part of the decision-making process.

Submissions to this Review supported the continued role of the Panel in the governance arrangements for determining the reliability standard and making recommendations to the AEMC in respect of the reliability settings.<sup>15</sup>

In 2011 the AEMC made a rule introducing a mechanism to index the market price cap and cumulative price threshold and a requirement for a four-yearly review of the reliability standard and reliability settings to be undertaken by the Panel.<sup>16</sup> This replaced the previous requirement of a two-yearly review of the reliability standard and reliability settings.

Also of relevance to the rule change request is the Reliability Panel's 2009 Review of Operational Arrangements for the Reliability Standard, which made a number of recommendations regarding the implementation of the reliability standard. These included that AEMO consider developing the ability to use dynamic joint regional reserve requirements to improve quality of information provided by medium-term PASA and that AEMO continue using the MRL process in the medium-term PASA as the primary method for assessing reliability in the medium-term.<sup>17</sup>

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<sup>14</sup> See chapter 7 of this Review.

<sup>15</sup> See Extreme Weather Review, Appendix I, available on the AEMC website.

<sup>16</sup> See National Electricity Amendment (Reliability Settings from 1 July 2012) Rule 2011 No. 5.

<sup>17</sup> See, Review of the Operational Arrangements for the Reliability Standard: Final Report, 21 December 2009.

### **3 Details of the rule change request**

This rule change request involves two distinct parts:

- the governance arrangements and determination processes for the reliability standard and reliability settings; and
- implementation of the reliability standard.

The details of these two parts of the rule change request are considered separately below, followed by the proponent's rationale for this rule change request.

#### **3.1 Proposed changes for determining the reliability standard and reliability settings**

This part of the rule change request proposes to:

- remove the Reliability Panel's (the Panel) responsibility for setting the reliability standard, and require the AEMC to take on this role;
- give the AEMC the power to determine certain reliability settings, including the Market Price Cap (MPC), the Market Floor Price (MFP), and the Cumulative Price Threshold (CPT), without the existing requirement for a rule change request from the Panel following its four-yearly review; and
- require the AEMC to develop guidelines it must follow in reviewing and setting the reliability standard and reliability settings (in accord with the Rules Consultation Procedures)

The reliability standard and reliability settings would be published by the AEMC in a reliability standard and reliability settings schedule.

The AEMC would also be required to conduct both a reliability standard review and a reliability settings review on a four-yearly basis in accordance with the rules consultation procedures and reliability standard and reliability setting guidelines.<sup>18</sup> These guidelines would set out the principles and assumptions to be applied by the AEMC in determining the reliability standard and settings under the proposed rule.

Both reviews are proposed to be conducted in consultation with the Panel, Registered Participants and other such persons the AEMC considers appropriate.

The reviews and guidelines are discussed further below.

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<sup>18</sup> See clauses 3.9.3B and 3.9.3C of the proposed rule.

### *Reliability Standard Review*

In conducting a reliability standard review under the proposed rule, the AEMC would be required to have regard to the same factors that the Panel must have regard to under the current arrangements, as set out in section 2.3. In addition to those factors, it would be required to consider the potential impact of any proposed changes on end-use customers.

Similarly, as under the current arrangements, if the AEMC determines to amend the reliability standard, it would be required to detail all relevant market conditions and circumstances on which the determination is based.

### *Reliability Settings Review*

Under the proposed rule, an AEMC reliability settings review would review the same parameters as the Panel does under the current arrangements; that is:

- the MPC, including the manner of indexing the MPC;
- the CPT, including the manner of indexing the CPT;
- the MFP; and
- the APC.

In conducting a reliability settings review under the proposed rule, the AEMC would be required to have regard to the same factors as for the proposed reliability standard review.<sup>19</sup>

As under the current arrangements, the proposed rule would also restrict the ability of the AEMC to determine an MPC or CPT to levels which the AEMC considers will:

- allow the reliability standard to be satisfied without use of AEMO's powers to intervene under existing clauses 3.20.7(a) and 4.8.9(a) of the NER; and
- in conjunction with other provisions of the NER, not create risks which threaten the overall integrity of the market.

The proponent also proposes to permit the AEMC to undertake a reliability standard review and a reliability settings review concurrently, or a reliability settings review only if the AEMC determines that no change to the reliability standard is necessary. The proponent's proposed rule also provides for the circumstance in which a reliability standard review is undertaken and no change to the reliability standard is determined, then no immediate review of the reliability settings would need to occur.

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<sup>19</sup> We note here there appears to be a drafting mistake in the proposed rule that omits the words "by AEMO" at clause 3.9.3C(c)(2) between the words "determined" and "which".

## *Reliability Standard and Reliability Settings Guidelines*

In its rule change request, the proponent proposes to introduce a requirement on the AEMC to develop a guideline, in accordance with the rules consultation procedure, that would set out the principles and assumptions to be applied by the AEMC in setting the reliability standard and reliability settings under the proposed approach.<sup>20</sup>

These guidelines are proposed to be capable of amendment by the AEMC as necessary and in accordance with the rules consultation procedures and would be required to be published and available at all times after their initial publication.<sup>21</sup>

### **3.2 Proposed changes to how the reliability standard is implemented**

This part of the rule change request proposes to:

- make AEMO responsible for making all reliability operational decisions, including to initiate the RERT, and to review/amend processes to assess the adequacy of generation reserves to meet the reliability standard; and
- require AEMO to develop, consult on and publish Reliability Standard Implementation Guidelines (RSIG) and Reserve Adequacy Requirements (RAR), which will act as parameters to guide and implement the reliability standard.

The proponent seeks to introduce a new requirement to the NER that would oblige AEMO to develop, in accordance with the rules consultation procedures, and publish Reliability Standard Implementation Guidelines (RSIG) that will function to:

- allocate responsibility to AEMO for determining a means of applying the reliability standard in every NEM forecasting timeframe it is required to address under the NER;
- provide flexibility for the reliability standard to be applied operationally through time and across different NEM forecasting timeframes so that it best suits the form of standard set and the circumstances to which it is being applied;
- set out a structure and process that AEMO must follow in establishing and changing the RSIG and associated RARs;
- allow AEMO to make changes to the NEM processes to adapt to any changes made to the reliability standard or reliability settings without the need for a rule change request; and
- transition from the current practice in which MRLs determined by AEMO become RARs and the methodology for determining them is set out in the RSIGs.

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<sup>20</sup> See clause 3.9.3D of the proposed rule.

<sup>21</sup> *ibid.*

Under the proposed rule, the RSIGs must specify a methodology for determining RARs for each forecasting timeframe. The RARs are proposed to be the primary output of the RSIGs and must include a description of how they are intended to be used, and detail the following matters:

- the approach used and the assumptions made in relation to the demand for electricity;
- the approach used and the assumptions made in relation to the reliability of existing and future generation;
- the approach used and the assumptions made in relation to intermittent generation;
- the approach used and the assumptions made in relation to energy constraints; and
- how network constraints are taken into account.

The proposed rule would enable AEMO to adjust the RARs as the power system changes, in accordance with the RSIGs.<sup>22</sup> The proponent indicates that the RARs would be implemented in tools used by AEMO to inform the market, such as short-term PASA, and would be published on its website.

AEMO would also be enabled to amend or replace the RSIGs in accordance with the rules consultation procedures.<sup>23</sup>

The proponent notes that although MRLs would be an example of RARs under the proposed approach, other forms of parameters may emerge as other techniques are developed.

### **3.3 Rationale for the proposed rule change**

In its rule change request, the proponent provides its rationale for the proposed rule change. A number of key points raised to support the rule change request are:

- to reduce uncertainty and improve transparency regarding the reliability standard and reliability settings review and determination processes, including the operationalization of these parameters;
- to maintain consistency and reduce complexity of the existing decision-making processes and to provide important signals for long-term investment in capacity by market participants; and

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<sup>22</sup> See proposed rule cl. 3.9.3E(d).

<sup>23</sup> See proposed rule, cl. 3.9.3E(g).

- to establish a clear allocation of responsibility for interpreting and applying the reliability standard in the context of the numerous market processes used in the NEM

The proponent argues that the proposed rule change will improve accountability, consistency and timing around the reliability standard and reliability settings review and determination processes and thereby enhance investor certainty.

The proponent considers the proposed rule better balances transparency, through clearer responsibilities and governance under the rules, and flexibility for arrangements to be changed under a well-defined process.

Specifically in respect of the development of the RSIG, the proponent considers benefits include:

- bringing the process of operationalising the reliability standard into the governance of the rules and clearly assigning AEMO with responsibility for doing this, instead of the rules being silent in relation to responsibility and governance;
- making the process of operationalising the reliability standard more transparent and engaging the market through consultation;
- allowing more flexibility for fit-for-purpose approaches to be used in various forecasting timeframes, where warranted; and
- using more accurate reliability measures as they are developed and creating a set of processes and parameters that can evolve over time.

## 4 Assessment framework

The Commission's assessment of this rule change request must consider whether the proposed rule promotes the (NEO) as set out under section 7 of the National Electricity Law (NEL).

Section 7 of the NEL states:

“The objective of this Law is to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to - (a) price, quality, safety, reliability and security of supply of electricity; and (b) the reliability, safety and security of the national electricity system.”

The Commission considers that the relevant aspects of the NEO for further consideration are the efficient investment in electricity services with respect to the price, quality, security and reliability of supply of electricity and the reliability and security of the national electricity system.

In assessing the rule change request against the NEO, the AEMC will consider whether the proposed rule satisfies the rule making test in that it will, or is likely to, contribute to the achievement of the NEO.

More broadly, we will also consider whether there is a problem to be addressed under both parts of the rule change request and whether the proposed rule is a proportionate response to any issues identified.

At section 4.1, we set out the proposed assessment framework to consider the proposed governance arrangement changes relating to the reliability standard and reliability settings.

At section 4.2, we set out the proposed assessment framework to consider the proposed changes to how the reliability standard is implemented by AEMO.

### 4.1 Proposed changes to the governance arrangements of the reliability standard and reliability settings

The Commission proposes to test the contribution of this part of the proposed rule to the promotion of the NEO by considering the impacts of the proposed rule on good governance principles and good regulatory practice.

Governance is the system or process by which organisations are directed, managed and interact with stakeholders. It also relates to the way in which decisions are made and an organisations' accountability for those decisions. Good governance practice is important for promoting investor confidence and efficient investment in the NEM.

Ultimately, efficient investment will affect the prices that consumers pay for their electricity and the reliability of their supply. In this part of the rule change request, we

are primarily concerned with good governance as it applies to the roles of the AEMC and the Reliability Panel in reviewing and determining the reliability standard and settings.

The following governance principles will guide our assessment:

- Principle 1 - to promote best natural fit - eg, which entity(ies) is best placed to decide on the level of the reliability standard and settings from both an accountability perspective and given the nature of their roles in the NEM?
- Principle 2 - to minimise conflicts of interest - eg, are there any actual or perceived conflicts of interest that may affect investor confidence?
- Principle 3 - to allow for proportionate regulation - eg, is the administrative burden no greater than necessary and is there an appropriate balance between regulatory certainty and flexibility?

The following questions are illustrative of the issues to be canvassed:

- Would the proposed approach affect investor certainty and confidence in the NEM and lead to more efficient or inefficient investment outcomes?
- Would the proposed rule increase or decrease accountability, transparency, certainty and stability in the NEM?
- Would the proposed approach promote administrative efficiency, minimise undue regulatory burden and foster efficient investment in and operation of the NEM?
- Is it appropriate to remove the reliability settings decision-making process from the rule change process?

The AEMC is currently processing the System Restart Ancillary Services (SRAS) rule change request, which considers the roles and responsibilities of the AEMC and the Reliability Panel in terms of the governance of the SRAS frameworks. The governance issues raised in the SRAS rule change request are similar to those raised in this rule change request. For this reason, the timing of these two projects has been aligned to allow for co-ordinated consideration of these issues.

Stakeholders may therefore wish to have regard to this in commenting on the proposed assessment framework.

#### **4.2 Proposed changes to how the reliability standard is implemented**

The Commission proposes to test the contribution of this part of the proposed rule to the promotion of the NEO through consideration of the impacts of the proposed rule on good governance principles and reliability and security of supply of electricity and the NEM.

As noted above, the proponent submits that the rule as proposed will reduce uncertainty and improve transparency regarding the reliability standard and reliability settings process, including how these parameters are implemented by AEMO. By requiring a single decision-maker to undertake these processes, the proponent argues that complexity will be reduced and important signals for long-term investment in capacity to market participants will be provided.

The proponent notes that AEMO currently uses tools and processes other than MRLs to apply the reliability standard operationally, including more probabilistic techniques that have been developed to better reflect the uncertainties that occur with increasing forecast timeframes.<sup>24</sup> The proposed changes to how the reliability standard is implemented by AEMO seek to formalise these developments through the requirement on AEMO to develop related guidelines governing these processes.

The rule change also seeks to provide AEMO with more flexibility to change the way in which it implements the reliability standard as it continues to refine or develop new techniques.

The proponent argues that the outcomes associated with the proposed changes are likely to have a positive impact on institutional accountability of the decision-making processes, as well as timeliness of decisions that affect the market, and, ultimately, consumers.

These propositions will be tested as part of the assessment of this rule change request.

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<sup>24</sup> See rule change request, 9 May 2013, p6.

## 5 Issues for consultation

Taking into consideration the assessment framework and the potential changes required to implement the proposed rule change, we have identified a number of issues for consultation.

The issues outlined below are provided for guidance. Stakeholders are encouraged to comment on these issues as well as any other aspect of the rule change request or this paper, including the proposed assessment framework.

### 5.1 Is there a problem to be addressed?

The proponent has raised a number of concerns with the existing reliability framework. The AEMC encourages stakeholders to consider first whether there is an issue that needs to be addressed and, if so, whether changes to the current framework are required, in respect of either the governance of the reliability standard and settings or the implementation of the reliability standard.

**Box 5.1: The issues as proposed**

1. Considering the issues raised in the rule change request, do you consider there is a problem with the NER that needs to be addressed through a rule change or may be addressed in some other way?

In doing so, stakeholders should consider the context of the 2010 Extreme Weather Review on which the rule change is based. The former MCE was concerned about the impact of possible increases of the frequency and or severity of extreme weather events in the NEM following supply interruptions in Victoria and South Australia due to a heat wave. The AEMC is seeking views from stakeholders on whether issues raised remain relevant.

In particular:

- Do the current governance arrangements, with separate decision making bodies for the reliability standard and reliability settings, restrict the ability of the NEM to respond efficiently to a possible increase in the frequency and/or severity of extreme weather events?
- Is there a lack of high level guidance in the rules for setting the reliability standard and reliability settings and, if so, does this lead to inefficiencies and restrictions on what information can be taken into account as part of the decision making process?
- Does the presence of existing market participants on the Reliability Panel give rise to perceived or actual conflicts of interest?

Note also that the AEMC has since made a rule introducing a mechanism to index the MPC and CPT, and a requirement for the Panel to undertake a four-yearly review of the reliability standard and reliability settings.<sup>25</sup>

## **5.2 Governance of the reliability standard and reliability settings**

To address the issues it identified in relation to the governance arrangements, the proponent has proposed to change the entity that determines the reliability standard as well as the statutory location of both the reliability standard and the reliability settings. These proposed changes would also impact the decision-making processes for reviewing and setting the standard and the reliability settings, including the way in which consultation occurs and the way in which decisions can be challenged.

In considering the impacts of the proposed changes or any other preferred solutions, stakeholders may therefore wish to consider the nature of the AEMC and the Reliability Panel's roles, including their governance arrangements and the frameworks and processes that guide their decision-making.

The Panel currently has a mixed advisory and determinative role. The proposed rule would change the Panel's role in respect of the reliability standard from being a determinative one to an advisory one. If this rule change request is implemented as proposed, the Panel would remain responsible for developing and publishing power system security standards and related guidelines.

The Panel currently plays, and will continue to play, an important role in executing these functions. The Panel's role in providing advice to the AEMC on the reliability settings, or possibly the reliability standard, will also remain an essential input due to the Panel's experienced and diverse membership of industry and consumer representatives.

In the context of this rule change request we are seeking views from stakeholders on whether:

- there are benefits in having a single governance arrangement for the reliability standard and the reliability settings;
- the Panel's role in setting the reliability standard should be advisory or determinative;
- it is more appropriate for the reliability standard to be determined under a Panel process, under rules-based process, or under a process that is developed in guidelines outside of the rules.

The following Box 5.2 sets out specific questions relating to the proposed changes.

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<sup>25</sup> See National Electricity Amendment (Reliability Settings from 1 July 2012) Rule 2011 No. 5.

**Box 5.2: The proposed changes to the governance arrangements**

1. Do you consider the proposed solutions are a proportionate response to the issues identified by the proponent? If not, do you think there is a more preferable solution(s) to the issues raised by the proponent?
2. Given the inter-linkages between the reliability standard and the reliability settings, would it contribute to the promotion of the NEO, or otherwise, to require a single decision-maker to determine both aspects of the reliability framework? Alternatively, are there any benefits to having the reliability standard and reliability settings determined by different entities?
3. Given the nature of the governance arrangements, role and decision-making processes of the AEMC and the Reliability Panel, which entity is better placed to decide on the reliability standard and the reliability settings?
4. Is it more appropriate for the reliability standard and/or the reliability settings to be set under a rules-based process or some other process?
5. How would each of the alternative governance arrangements affect investor confidence in the NEM?
6. How might alternative governance arrangements affect other market participants and, ultimately, consumers?
7. What costs and benefits, both direct and indirect, might arise from changes to the governance arrangements?

### **5.3 Implementation of the reliability standard**

The rule change proponent is concerned that AEMO is currently constrained in its ability to use more sophisticated techniques for managing the reliability standard. This is because the rules currently have obligations for AEMO to determine short-term and medium-term reserve requirements, however there is no process set out in the rules for AEMO to determine these requirements.

The proponent considers that it is important to set down a clear allocation of responsibility for interpreting and applying the reliability standard. The proponent also considers AEMO should have the flexibility in the way that it implements the reliability standard. The proponent's views on the benefits of this approach are set out in section 3.3.

The AEMC is seeking feedback from stakeholders on how the proposed changes to the way in which AEMO implements the reliability standard will affect market participants and ultimately consumers. Specific questions are set out in Box 5.3.

**Box 5.3: The proposed changes to implementing the reliability standard**

1. Would increased flexibility in the way in which AEMO implements the reliability standard improve investment, security, and reliability outcomes in the NEM?
2. Would transparency and certainty be increased, or otherwise affected, by the proposed AEMO-developed guidelines (RSIG) and parameters (RAR) that would guide and describe the techniques used by AEMO to implement the reliability standard?
3. Would the proposed changes affect investor confidence in the NEM? If so, please characterise.

## **6 Lodging a submission**

The Commission has published a notice under section 95 of the NEL for this rule change proposal and inviting written submissions. Submissions are to be lodged online or by mail by 23 October 2014 in accordance with the following requirements.

Where practicable, submissions should be prepared in accordance with the Commission's guidelines for making written submissions on rule change proposals.<sup>26</sup> The Commission publishes all submissions on its website, subject to legal requirements relating to confidentiality.

All enquiries on this project should be addressed to Matt Lady on (02) 8296 7800.

### **6.1 Lodging a submission electronically**

Electronic submissions must be lodged online via the Commission's website, [www.aemc.gov.au](http://www.aemc.gov.au), using the "lodge a submission" function and selecting the project reference code "ERC0160". The submission must be on letterhead (if submitted on behalf of an organisation), signed and dated.

Upon receipt of the electronic submission, the Commission will issue a confirmation email. If this confirmation email is not received within three business days, it is the submitter's responsibility to ensure the submission has been delivered successfully.

### **6.2 Lodging a submission by mail**

The submission must be on letterhead (if submitted on behalf of an organisation), signed and dated. The submission should be sent by mail to:

Australian Energy Market Commission  
PO Box A2449  
Sydney South NSW 1235

Or by facsimile to (02) 8296 7899.

Please clearly mark the envelope or facsimile with the project reference code: ERC0160.

Except in circumstances where the submission has been received electronically, the Commission will issue a confirmation letter upon receipt of the hardcopy submission.

If this confirmation letter is not received within three business days, it is the submitter's responsibility to ensure successful delivery of the submission.

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<sup>26</sup> This guideline is available on the AEMC website.

## Abbreviations

AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AFP	administered floor price
AMPR	annual market performance review
APC	administered price cap
COAG	Council of Australian Governments
Commission	See AEMC
CPT	cumulative price threshold
MCE	Ministerial Council on Energy
MFP	market floor price
MPC	market price cap
MRL	Minimum Reserve Levels
NEL	National Electricity Law
NEM	National Electricity Market
NEO	national electricity objective
PASA	Projected Assessment of System Adequacy
RAR	Reliability Adequacy Requirements
RERT	reliability and emergency reserve trader
RSIG	Reliability Standard Implementation Guidelines
SCER	see COAG Energy Council
USE	unserved energy