

28 April 2006

Dr John Tamblyn
Chairman
Australian Energy Market Commission
PO Box H166
AUSTRALIA SQUARE NSW 1215

Attention: Mr Tendai Greegan

Dear John

Management of Negative Settlement Residues in the Snowy Region - Implementation Timing

I refer to the Commission's request, of 20 April 2006, for a response from NEMMCO on two matters relating to the possible implementation of the proposed National Electricity Amendment (Management of negative settlement residues in the Snowy Region) Rule. After considering those matters and the Commission's extended timeframe for release of a draft determination, NEMMCO offers the following comments relating to implementation of the proposal. In addition, NEMMCO asks the Commission to consider an appropriate expiry date for the related derogation, which is currently 31 July 2007, in the context of the congestion management review currently being undertaken by the Commission.

1. System Development Timeframes

The implementation time to accommodate a new process to determine settlement residue on the Victoria to Snowy interconnector is set by the period required to develop, test and release new software to manage the efficient settlement of the new Rule.

The current CSC/CSP process for the Snowy Region is performed by a specialised external process that has been developed external to the main Market Management Systems (MMS). This external process was developed as an emergency implementation due to the tight deadlines required and the uncertainty as to whether it was to be implemented. NEMMCO is currently working to integrate this process into the MMS in time for the summer of 2006/07. This brings greater consistency in the maintenance, documentation, unit and system testing and change management. The MMS upgrade cycle has been agreed with NEM Participants to be 6 monthly with an additional lead time of 3 to 9 months depending how well defined the change proposal is and the point of commencement in the update cycle. The operation and support of market processes implemented in systems outside of the main MMS is not good business practice and runs increased risk of audit and stability issues.

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Participants would also require time to make changes to their business support and reconciliation systems.

The Commission has announced it intends to publish a draft determination by mid May 2006, and on this basis NEMMCO would anticipate a final determination by around August 2006. In order to accommodate the early introduction of the proposed Rule, NEMMCO would initially be prepared to work to develop the design on the basis of the draft Rule determination. After considering the timing with respect to the current MMS release cycle, the earliest that a new process to determine settlement residue on the Victoria to Snowy interconnector could be delivered, based on a mid May draft determination, would be 1 December 2006. If the final Rule determination was materially different to the draft, the implementation date would need to slip to 1 June 2007. However, this is only two months before the derogation expires (see section 3 below). The implementation could slip further if the Commission were to extend the timeframe for determining the Rule.

If the final Rule were to require a change to the design based on the draft determination, and implementation was required before 1 June 2007, NEMMCO's only option is the undesirable development of external and adhoc systems, which is not recommended. The earliest implementation date under this scenario, for say an August/September determination, would be mid February 2007.

2. Settlement Residue Auction Timeframes

When a Rule or process change is determined that changes the method of calculation of settlement residue, under the Auction Participation Agreement, Auction Participants may terminate any Settlement Residue Distribution Units (SRDU) which they have obtained with respect to impacted future periods. It is anticipated that the proposed modification to the management of negative residues on the Victorian to Snowy interconnector would constitute such a change for Victorian to Snowy, and Snowy to NSW directional interconnectors.

Where units have been terminated and returned by an Auction Participant with sufficient notice prior to the last tranche auction of the relevant quarter, NEMMCO would be able to re-auction any returned units along with the standard 25% quota before the start of the relevant quarter.

The timing would also need to ensure sufficient lead time for participants to be made aware of the material change, so that they can determine their position. In practice, this means that after a Rule change that impacts the calculation of the settlement residue:

- NEMMCO would invite participants to advise their intention with regard to termination (7 days)
- Participants to advise NEMMCO of their intentions in say 14 days
- NEMMCO to notify units for sale at least 10 business days before the auction in accordance with the auction rules
- Auctions held mid March, June, September and December for the last opportunity to auction units in quarters that commence in April, July, October and January respectively.

Thus if units are to be able to be resold the Rule determination would need to be finalised at least two months before the commencement of the first impacted quarter. As long as there is two months' notice ahead of the start of the relevant first impacted calendar quarter, there is no particular reason to commence on a calendar quarter boundary.

If the two months' notice is not given the units would not be resold and the settlement residue would be directly paid to the relevant TNSP.

Thus by way of example, if the Rule change was determined by 1 November to commence on 1 January, this would allow SRA units to be resold. A Rule determined on say 15 September for a 1 December start would not allow units to be resold.

3. Expiry of the network constraint formulation derogation

The derogation Part 8 Network Constraint Formulation of chapter 8A of the Rules has three functions:

- clarifies NEMMCO's authority to use fully co-optimised network constraint formulations;
- allows NEMMCO to manage counter-priced inter-regional flows using alternative constraints formulations; and
- implements the Snowy CSC/CSP trial.

Under clause (e), the derogation expires either on 31 July 2007, the implementation of the first regional boundary review by the Commission, or as otherwise determined by the Commission. NEMMCO also understands that the Commission is planning to release the final report of its review in congestion management in September 2007. Allowing for any subsequent consideration by the Ministerial Council on Energy, changes to the Rules by the Commission and implementation by NEMMCO, there could be 18 months between expiry of the derogation and implementation of the outcomes of the congestion management review.

On this basis, NEMMCO believes it would be prudent for the Commission to consider an appropriate expiry date for the derogation as part of its determination on the Management of Negative Settlement Residues in the Snowy Region proposal.

Yours sincerely


Brian Spalding
Chief Operating Officer