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20 September 2010

Commissioner Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

By email: submissions@aemc.gov.au

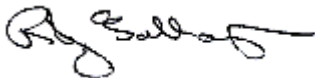
Dear John

EPR0019: AEMC Transmission Frameworks Review

Please find attached a brief submission in response to your Issues Paper dated 18 August 2010.

I would be pleased to discuss any of the matters raised in this submission with you or your staff if you wish.

Kind regards



Director

Att.

AEMC Issues Paper: Transmission Frameworks Review

Responses to the AEMC's Questions

No	Question	Response
1	Application of NEO	<ul style="list-style-type: none"> • Absolute minimisation of total system costs or maximisation of economic efficiency is unattainable. As an objective, this grossly oversimplifies the problem of planning for uncertainty. In this regard, we are not only dealing with market and cost based uncertainty but also the many unknowns in relation to the technical, commercial, environmental and political risks and constraints that will impact over time on the merits of any particular near term TX investment proposal. • No market is perfect and the NEM is no exception. A critical issue however in the design of any market and its overarching governance, however imperfect it may be, is how the risks of poor decisions and/or poor performance are allocated amongst all the various stakeholders. • Therefore a good place to start the Review would be to look at how the spirit and intent of the NEO has thus far been interpreted in the current transmission planning and investment decision-making processes in the NEM, and how it should be interpreted and applied in the long term future. As a key component of this, the Review should reconsider how the risks of poor TX investment decisions and/or poor TX operational performance are allocated, and whether this is impeding or supporting the overall pursuit of the NEO. • In my view, to the extent that we need to retain centralised planning of the grid, we need to move to a probabilistic planning methodology, and one that is considerably more sophisticated than the one currently used by AEMO for Victorian TX network planning. • Another key issue for the Review to consider in this respect is the very different access regimes for gas and electricity transmission and the potential for this to systemically bias future TX investment in the electricity grid rather than the gas network which is clearly the more economic option where one can readily substitute for the other.
2	The Role of Transmission	<ul style="list-style-type: none"> • The first issue to consider is the extent to which the provision of TX services should remain a regulated monopoly, who should make the investment decisions for the provision of those services, and how the various risks associated with those investments should be allocated. • Even within the existing NEM framework, provision of TX services in Victoria has more competitive elements than is the case in other States. • However, we should be investigating the feasibility of moving to a much broader competitive market model for the provision of such

No	Question	Response
		<p>services and the improved allocation of market risk that it would entail.</p> <ul style="list-style-type: none"> The underlying philosophy of energy industry reform in Australia has long been to rely on market forces combined with general competition law and light-handed regulation where possible, and only resort to the provision of regulated monopoly services where a proper functioning market is infeasible or impractical for whatever reason. The need to continue to treat the provision of the great majority of TX services as a natural monopoly should be revisited.
3	Transmission Planning	<ul style="list-style-type: none"> Under the current TX planning regime, TNSPs bear no investment risk, they are allowed to use simplistic planning standards and methodologies (particularly in terms of how they deal with future uncertainty), and quite understandably, their planning and investment decision-making processes are primarily focused on “managing” the regulatory process to protect their revenue streams and regulated ROI. Within this framework, market-based signals currently play a very limited role. There is near universal acceptance that markets and market-based signals are a superior alternative to provision of services by regulated monopolies wherever feasible, and this was the driving force behind much of the electricity industry and market reforms of the past 2 decades in Australia. The question therefore should be “Would it be feasible to use market-based signals to drive a lot more TX services related investment and operation in the NEM thereby reducing the breadth and scope of the role played by regulated monopoly service provision?” The second question then is “To the extent that TX services should continue to be provided by regulated monopoly service providers, to what extent is it appropriate to allow the provision (or lack thereof) of those services to impact on competitive market outcomes, given the commercial risks that this imposes on market participants and the limited options available to them to manage those risks?”
<p>As a general comment, the remaining 7 questions deal with a narrow sub-set of issues that should be left in abeyance until the Review has dealt with the much broader issues outlined above and the future direction for further reform, if any, of the TX framework is established. If any significant change to the current TX framework is to occur, it will come from the Review's consideration of the broader issues. All of the AEMC's remaining questions and any perceived need for change arising from those considerations could be addressed within the current framework, as has been occurring on a more or less continuous basis (with limited success) for the past 15 years.</p>		
4	Promoting Efficient Transmission Investment	<ul style="list-style-type: none"> It is impossible to predict whether or not the current framework will deliver efficient and timely investment in new TX facilities because it is susceptible to being manipulated by Governments, TNSPs and stakeholder groups alike in pursuit of their own objectives and sectional commercial and non-commercial interests.

No	Question	Response
5	Economic Regulation of TNSPs	<ul style="list-style-type: none"> • Economic regulation of TNSPs should incentivise them to pursue outcomes for the TX sector that are consistent with so-called “optimum” market outcomes for the entire supply chain. • While TX investment is an important component, other key elements of the full range of TNSP activities should not be ignored.
6	Network Charging for Generation and Loads	<ul style="list-style-type: none"> • Clearly, generators should see an effective TX related price signal for all new generation investments as well as for both temporary and permanent plant withdrawal / mothballing / retirement decisions. The impact such a signal would have on loads depends entirely on how it was designed and implemented.
7	Nature of Access	<ul style="list-style-type: none"> • To the extent that it is feasible to vary the level of service to one individual network user without impacting on the service level of other users, then it should be the commercial decision of the user as to the level of service it wishes to buy.
8	Connection Arrangements	<ul style="list-style-type: none"> • This is a less important issue. Notwithstanding, it should be revisited after the more important question of access arrangements for the shared network have been addressed.
9	Network Operation	<ul style="list-style-type: none"> • The need for increased accountability for TX owners and operators re their performance and the impact it has on market outcomes is clearly required. This includes AEMO as well as NSPs.
10	Dispatch of the Market and Management of Congestion	<ul style="list-style-type: none"> • The key to enhanced congestion management is to improve congestion pricing in the market. The long term trend in the NEM will be towards more diverse generation types, more distributed generation embedded in the sub-transmission and distribution systems, more intermittent and must-run generation technologies, and, on the customer side, increasing value being placed on the quality and reliability of supply. • The NEM should be providing appropriate real time price signals to all dispatchable generation sources and loads; price signals that are not distorted by unduly low price caps, zonal pricing approximations, inter-temporal price averaging or ex-post price adjustments, all of which detract from the overall integrity of the market. • At the same time, all constraints impacting on real time dispatch should be defined as accurately as possible in real time, and where they are movable, the price of moving those constraints should be quite explicit and factored into market price outcomes. The current NEM dispatch process falls a long way short of this. While the current model was a pragmatic basis on which to launch the NEM more than 10 years ago, the adverse effects of its many deficiencies are growing with the changes now occurring in the market.