

National Electricity Market - Regional Structure

Terms of Reference

27 January 2004

Background

The future framework for transmission is a significant and pressing market reform issue in the National Electricity Market (NEM) and Ministers, both through the NEM Ministers' Forum and the Ministerial Council on Energy (MCE), have recognised the importance of providing a clear and stable framework for transmission development.

In light of concerns that existing transmission measures may not deliver the level of reliability and investment sought, NEM Ministers agreed in July 2002, to develop a policy framework for the future development of transmission.

Consistent with their policy oversight role, the NEM Ministers requested a moratorium on the investigation and progressing of all transmission and regional boundary issues by the NEM institutions. The rationale for the moratorium was to align all existing reviews pertaining to transmission and regional boundaries and ensure the implementation of a holistic policy framework moving forward.

The NEM institutions agreed to this request and the moratorium remains in place.

It is recognised that while the MCE has agreed that jurisdictional boundaries should be maintained for retail customer pricing, economic benefits may exist in changing arrangements at the wholesale level.

Substantial work has been undertaken towards developing an efficient and effective framework for transmission development. On 11 December 2003, the MCE in its report to COAG on Energy Markets¹, adopted four principles to underpin transmission policy in the NEM:

1. The transmission system fulfils three key roles – it provides a transportation service from generation source to load centre, facilitates competition, and ensures secure and reliable supply.

¹ Ministerial Council on Energy Report to Council of Australian Governments on Reform of Energy Markets - 11 December 2003.

2. There is a central and ongoing role for the regulated provision of transmission, with some scope for competitive (market) provision.
3. Transmission investment decisions should be timely, transparent, predictable and nationally consistent, at the lowest sustainable cost.
4. The regulatory framework should maximise the economic value of transmission, including through the efficient removal of regional price differences in the operation of the NEM.

Within these principles, the MCE agreed to a package of initiatives addressing seven key transmission issues.

Included in these initiatives was a recommendation for:

“A new process to be developed for assessing wholesale market regional boundaries, while maintaining jurisdictional boundaries for retail customer pricing.”

The MCE has agreed that while jurisdictional boundaries should be maintained for retail customer pricing, a new and more transparent process (managed by the AEMC) is required to enable assessment of regional boundary changes for the wholesale market to facilitate investment and more efficient operation of the NEM while maintaining a secure power system.

To enable this framework to be developed, the MCE has further agreed:

- to commission an independent economic study to develop the criteria and process for boundary changes, and initial boundary change options, reporting to the MCE by June 2004;
- that the boundary change process developed must include sufficient lead time to address commercial and economic considerations; and
- that the independent economic study will include wide market consultation.

Review requirements

Experience in the operation of the market has revealed significant concerns with both the Code criteria for regional boundaries and the process for implementing boundary changes. The current criteria are too rigid and fail to adequately address economic or commercial considerations.

The purpose of the economic study will be to:

- Review and develop proposed regional boundary criteria and means of managing network congestion consistent with the policy direction set by MCE.

- Develop options on a mechanism for changing wholesale regional boundaries or other means of transparently and consistently managing network congestion in the NEM.
- Recommend a revised mechanism for wholesale regional boundaries and the criteria underpinning it, having regard to the objectives outlined below.
- Provide a basis to enable the AEMC to progress changes to the Code to implement a revised mechanism for wholesale regional boundary changes.

In this regard, there are currently several potential options for changing the wholesale structure of the NEM including but not limited to:

- Work undertaken by NEMMCO, including on constraint formulation;
- Previous CRA study which developed a “gatekeeper” proposal;
- A proposal to examine nodal pricing for generators.

In developing a revised framework, there are potentially competing objectives including:

- Managing retail price outcomes;
- Ensuring efficient dispatch of generation;
- Ensuring the maintenance of a secure and reliable power system;
- Transparent and consistent application of the process across the NEM;
- Efficient and predictable basis for investment;
- Mitigating the scope for an exercise of market power;
- Financial market liquidity and risk management;
- Efficient usage of the transmission system.

To fully scope the required issues to take into account in developing a new mechanism, an industry forum will be conducted at the start of the consultancy.

The study will inform further consideration and development of enhanced inter-regional trading arrangements. Accordingly, the consultant should identify enhanced inter-regional trading arrangements where they support the mechanisms for wholesale regional boundaries presented.

Process and timetable

The consultant will be required to work closely with the Standing Committee of Officials (SCO), which is responsible to the MCE. It is envisaged that there will be a series of regular meetings with SCO representatives throughout the course of the consultancy to discuss project progress and obtain feedback.

There is an expectation that key reporting and deliverable dates will be strictly adhered to. These include:

- Commencement of consultancy – by 23 February 2004.
- Overview of approach methodology – by 8 March 2004.
- Jurisdictional feedback on methodology – by 16 March 2004.
- Industry forum commencing mid-March to late-April 2004 to identify and scope the key issues to be addressed in draft report. The industry forum will involve:
 - date to be set and industry to be notified well in advance by the SCO Secretariat;
 - formal presentations to be made by representatives of industry sectors and market participants;
 - forum papers to be circulated in advance;
 - opportunity for facilitated open discussion.
- Draft Report to SCO outlining economic analysis, proposals and preliminary recommendations – by 10 May 2004.
- Draft Report discussion and feedback from jurisdictions – by 21 May 2004.
- Formal consultation with market on Draft Report seeking written submissions from interested parties – commencing 7 June 2004.
- Finalisation of the economic consultancy through a Final Report after discussion and feedback from jurisdictions – by 16 July 2004.

The SCO will provide a report and any recommendations to the MCE.

Consultant response to Terms of Reference

Consultants are asked to provide written response to this Terms of Reference providing the following details:

- Outline of the consultant's capability and relevant experience, including identification of the personnel directly involved in this assignment.
- Overview of the proposed approach, including a clear statement of the methodology that would be used.
- An indication of the key issues that will be covered in the analysis and their importance in determining the way forward for the development of a future framework for the assessment of regional boundary changes.
- A fee proposal, including a capped fee for the scope of work in the terms of reference, and a daily fee rate.
- Declaration of actual or potential conflicts of interest that may prevent or otherwise impede the consultant undertaking this assignment.

That consultancy proposal should be no more than 10 pages in total.

Any queries regarding the consultancy should be directed to Loretta Boman, Manager – Electricity & Markets, Office of Energy on 07 3224 6927.

Consultancy proposals should be addressed to:

Jill McCarthy
Ministerial Council on Energy Secretariat
Department of Industry, Tourism and Resources
Level 3
51 Allara Street
CANBERRA CITY ACT 2601
Ph: 02 6213 7789

Emailed responses are preferred and should be forwarded to:

MCE@industry.gov.au

Consultancy proposals must be received no later than 16 February 2004.