
Energy Market Reform

Industry Consultation Sessions

Sydney, 23 March 2004

Melbourne, 24 March 2004

Overview

- Progress since December 2003
- Current and future consultation program
- Streamlined code change process
- ACCC – AER – AEMC MoU
- Industry levy

MCE Reform Program

Agreed in December 2003:

1. Governance of energy markets
2. Economic regulation
3. Electricity transmission
4. User participation
5. Natural gas penetration

Implementation in 2004-06

Implementation - Management

- Governance and Institutions [SA, NSW]
- Economic Regulation [Vic]
- Electricity Transmission [Qld]
- User Participation [Tas]
- Gas Market Development [NT]

- Program Coordination [Cw]

Progress: Governance & Institutions

- Legislation: draft IGA and drafting instructions
- Levy: issues paper
- Code Change: streamlining position paper
- ACCC-AER-AEMC cooperation: MoU framework
- NECA: wind-up issues

Next Steps:

- Finalise IGA (MCE meeting 2 April 2004)
- AER and AEMC Members (May 2004)
- Commonwealth, state/territory legislation (June 2004)

Progress: Economic Regulation

- Access: evaluation criteria for national access regime
- Distribution & Retail: consultancy to stocktake existing regulatory regimes, analyse differences

Next Steps:

- Options for national access regime (initial consultation in August 2004, after PC Gas Access Regime Report)
- Issues paper on national distribution and retailing framework (initial consultation in July 2004)

Progress: Electricity Transmission

- Annual National Transmission Statement: commissioned NEMMCO to scope and develop
- Regional Boundaries: consultancy to review regional criteria and change process options
- Reg Test and Incentives: working with ACCC

Next Steps:

- ANTS overview (April 2004); first ANTS (July 2004)
- Regional boundary review report (June 2004)
- Draft transmission code changes (June 2004)

Progress: User Participation

- Demand-Side Response:
 - Interval Metering:
 - Retail Price Caps:
- } discussion paper

Next Steps:

- Industry workshops and responses (April 2004)
- MCE policy consideration (June 2004)

Progress: Gas Market Development

- MCMPR consideration of upstream issues
- Draft PC Report on Gas Access Regime
- Reviewed scope of gas market program

Next Steps:

- MCE review of gas program scope (April 2004)
- Gas market policy framework (tba)
- MCE response to final PC Report (late 2004)

Implementation - Consultation

- All stakeholders, supply & demand side
 - association and company level
 - current market institutions
- MCE website
 - papers, consultation information
 - e-mail newsletters
- Position and discussion papers:
 - written submissions
- Stakeholder workshops and briefings

Current Consultations

- **User Participation**
 - discussion paper released 12 March
 - industry workshops on 6-7 April
 - written submissions due 16 April
- **Code Change, MoU Framework, Levy**
 - discussion papers released 19-22 March
 - industry briefings 23-24 March
 - written submissions due 7 April
- **Regional Boundary Review**
 - Terms of Reference released 27 January
 - industry forum 31 March

Next Consultations

- Intergovernmental Agreement (tba)
- Regional Boundaries (June 2004)
- Transmission Code Changes (June 2004)
- Distribution and Retailing (July 2004)
- Access Arrangements (Aug 2004)
- Gas Market Development (tba)

AER – AEMC – ACCC MOU Framework

Overview

- MCE decision and MoU objectives
- MoU coverage
 - Roles of AER members and staff
 - Information exchange
- Legislative requirements
- Key elements of the MoU
 - Including the rule making protocol.

MCE Decision (1)

- Two new statutory commissions
 - AEMC for rule-making
 - AER for market regulation
- AER to be a constituent part of the ACCC
 - But operate as a separate legal entity

MCE Decision (2)

- ACCC retains responsibility for competition regulation
 - But will have a discretion to rely on AEMC processes when assessing applications for rule authorisations or access code acceptance under the TPA
- A Memorandum of Understanding (MoU) to be developed between the AEMC, the AER and the ACCC

MoU Purpose

- To define arrangements between the AEMC, the AER and the ACCC for
 - Consultation
 - Code change authorisation and acceptance
 - Information exchange
 - Staffing arrangements

MoU Objectives

- Efficient use of energy market expertise of AER for
 - Streamlining the changes to the codes
 - Informing the enforcement and administration of the TPA
- Provision of expert assistance to the ACCC on
 - Decisions on rule authorisation and acceptance of code changes in the energy market
 - Energy-related Part IV matters such as mergers and acquisitions

Role of AER/AEMC Members on TPA Matters

Code change authorisation or approval	Other TPA energy market matters
<p>Consultation between the ACCC and the AEMC will be necessary to ensure that industry-specific rule-making by the AEMC is directly influenced by the competition perspective of the ACCC.</p> <p>AER members may provide informal advice to the ACCC on matters relevant to code change decisions.</p>	<p>The ACCC may seek the formal advice of AER members on the administration and enforcement of the TPA in respect of particular energy matters.</p> <p>The ACCC may also seek the advice of the AEMC on such matters, particularly those which have implications for or interact with the AEMC's market development function.</p>

Role of AER Staff on TPA matters

Code change authorisation or approval	Other TPA energy market matters
<p>AER staff may/will participate in or undertake the drafting of advice to the ACCC on code change authorisations or approvals.</p> <p>The role of the AER staff in such matters will be by agreement between the ACCC and AER CEOs.</p>	<p>AER staff may participate in the drafting of advice to the ACCC on the administration and enforcement of the TPA in respect of particular energy market issues.</p> <p>The role of the staff in such matters will be by agreement between the ACCC and AER CEOs.</p> <p>There is no policy principle preventing AER staff from leading such work. The principal issue is for the AER to ensure that its statutory functions are adequately resourced.</p>

Information Exchange

- ACCC and AER
 - No limitation between both entities (AER is constituent part of ACCC)
 - Limitations on disclosure to third parties (other than AEMC)
- AEMC and AER/ACCC
 - No limitation between entities (to assist each to undertake its functions)
 - Limitations on disclosure to third parties

Legislative Requirements

- Consultation and decision processes for AEMC and AER
- Functions of AEMC and AER
- Information gathering powers
- Information disclosure limitations
- ACCC discretion to rely on AEMC processes
- Staffing of AER by secondment from the ACCC

Key Elements of the MoU

- Recitals, purpose and amendments
- Information gathering and sharing
- Rule making protocols (see next slide)
- Recruitment and staffing arrangements
- Cost recovery

Rule making

- AEMC will provide the ACCC and AER with any rule change proposal and related submissions
- AEMC will consult on relevant TPA questions (see consultation paper)
 - Sufficient to enable the ACCC to rely on AEMC processes
- AEMC will confer with ACCC on any competition or access related matter in a proposed rule change and seek to address all issues identified by the ACCC
- AER will advise the AEMC of any regulatory issues it identifies
- The AEMC will confer with the ACCC when making its final decision on whether to seek authorisation or access code approval

Summary

- The MoU will provide transparent arrangements for the inter-action of the AEMC and AER/ACCC, including
 - The objectives of the interaction
 - How they will consult and communicate on rule making and regulation
 - The processes that will be followed in the relationship between them
 - Staffing and resource-sharing

Streamlining the Energy Code Change Process

Industry Consultation
23 & 24 March 2004

Ministerial Council on Energy Report to COAG

Two new statutory commissions to be established on 1 July 2004, funded by industry levy:

- Australian Energy Market Commission (AEMC), with responsibility for rule-making and market development;
- Australian Energy Regulator (AER), with responsibility for market regulation.

Ministerial Council on Energy

Report to COAG

- The new regulatory arrangements to provide for consultation and cooperation between the AEMC, AER and ACCC.
- The code change and authorisation process to be streamlined, to avoid duplication.
- The AEMC and AER to have specific consultation obligations.
- End-user and industry consultation in developing code changes to be strengthened.

Overview of the Code Change Process

STEP 1

- Initiation of the code change process.
- Initial assessment by AEMC.
- AEMC notifies ACCC and AER of a code change proposal.

Overview of the Code Change Process

STEP 2

- Initial informal feedback from ACCC and AER.
- AEMC categorises the code change proposal.
- AEMC issues notice of proposed code change.

Overview of the Code Change Process

STEP 3

- AEMC calls for submissions.
- AEMC establishes working groups if required.
- AEMC holds public forum if requested.
- AEMC undertakes analysis.

Overview of the Code Change Process

STEP 4

- AEMC draft determination.

STEP 5

- AEMC calls for second round submissions.
- AEMC reconvenes working groups if required.
- AEMC holds pre-determination conference if requested.

Overview of the Code Change Process

STEP 6

- AEMC's Final Determination.
- AEMC confers with ACCC and the AEMC decides whether to refer the code change proposal to the ACCC for authorisation or approval.

Who can initiate a code change?

- Code participants
- Energy Market Institutions
- Governments
- Any other person

Content of a code change proposal

- Statement of problem in existing code
- Proposed code change solution
- How the code change will address the problem
- Prima facie demonstration of a net benefit
- Prima facie demonstration that proposal is consistent with “Prescribed Criteria”

Prescribed Criteria for assessing code change proposals

- MCE Policy Framework
- The Market Objectives

AEMC Preliminary assessment

Amending a code change proposal

- The proposal is not adequately developed
- The proposal requires amendment to overcome potential anti-competitive or trade restrictive matters

AEMC will not alter the proponent's original intent and the amendment must be a material improvement over the original.

AEMC Preliminary assessment

AEMC rejecting a code change proposal:

- If MCE does not approve consideration of a change to a protected provision
- Proposal is not adequately developed and cannot be readily amended
- No possible benefit to outweigh any anti-competitive or trade restrictive matters

AEMC Preliminary assessment

AEMC rejecting a code change proposal (cont.):

- No demonstration of prima facie benefit
- Frivolous or mischievous behaviour
- Proposal is inconsistent with “Prescribed Criteria”

Initial involvement of ACCC and AER

- ACCC will advise AEMC on any competition or access issues arising from proposal
- AER will advise AEMC on any regulatory or enforcement issues arising from the proposal

Categories of code change

- **Category 1**- minor or administrative nature, which can be fast tracked
- **Category 2** – no significant competition or access issues and can be expedited (subject to no objection)
- **Category 3** – have significant competition or access issues and requires full consultation
- **Category 4** – affects protected provision and requires full consultation and sign-off by MCE

Process for dealing with Category 1 changes

- AEMC will publish its decision to categorise the code change as Category 1
- If anyone disputes the categorisation within 14 days, AEMC will re-categorise and follow relevant process
- If no objection, AEMC can make a final determination and gazette change

Calls for submissions

AEMC will identify issues raised by ACCC and/or AER and seek submissions on whether the code change proposal:

- Might result in contravention of TPA
- Would be likely to result in anti-competitive detriment
- Benefit would outweigh anti-competitive detriment
- Would result in a variation to an access code
- Is consistent with the “Prescribed Criteria”

AEMC analysis of proposal

- The AEMC will undertake economic, legal or engineering analysis of a material Code change proposal.
- The AEMC will undertake any analysis required to seek to address the competition, access or regulatory issues raised by the ACCC and AER respectively.
- The AEMC will have the discretion to publish its analysis and call for submissions on the analysis.
- In any event the analysis will be included as part of the AEMC's draft determination.

AEMC draft determination

The AEMC will publish a draft determination of a code change proposal, which will include:

- Assessing the proposal against the “Prescribed Criteria”
- Amending the wording to address concerns raised through consultation
- Address all material issues raised in consultation
- Address all issues raised by ACCC and/or AER
- Foreshadowing whether to refer the change to ACCC
- Assessing net benefits
- Draft decision of whether to approve change and reasons

Second Round submissions

- The AEMC will call for second round submissions following publication of the draft determination.
- The AEMC will reconvene working groups if required.

Expedited code change

The draft determination will automatically become the final determination if no one registers an intent to make a second round submission within two weeks of the AEMC publishing its draft determination.

Pre-determination conference

- Interested parties have the option to call for a pre-determination conference.
- The pre-determination conference provides the opportunity for the AEMC to explain the draft determination and/or the analysis and provide interested parties with an opportunity to ask questions before submitting their second round submissions.

Final determination

The AEMC will publish a final determination of a code change proposal, which will include:

- Assessing the proposal against the Prescribed Criteria
- Address all material issues raised in comments and submissions on draft determination, including those raised by ACCC and AER
- Address substantive issues raised in the pre-determination conference
- Assessing net benefits
- Final decision of whether to approve change and reasons

Referral of code changes to ACCC

- The AEMC will manage the code change process.
- The AEMC would have the discretion to apply to the ACCC for authorisation for competition-related code changes or approval of access-related code changes.
- The ACCC has the discretion to rely on the submissions provided to the AEMC.

Timeframe for the code change process

Step 1	Initial assessment of proposal Refer proposal to ACCC/AER	2 weeks
Step 2	Feedback from ACCC/AER Categorisation by AEMC	2 weeks
Step 3	Seek submissions Working groups and Public forum AEMC analysis	1 to 3 months (add 1 month if submissions on analysis called)
Step 4	Draft determination	1 month
Step 5	Second round submissions Working groups if required Pre-determination conference	1 month (add 1 month for conference)
Step 6	Final determination	1 month

Your input

Submissions on the *Streamlining the energy code change process* consultation paper should be forwarded to:

MCE Secretariat

Department of Industry, Tourism and Resources

GPO Box 9839

Canberra

ACT 2601

Discussion Paper

Application of the Industry Levy to Fund the AER and AEMC

Overview

- Introduction
- Background & Objectives
- Economic & Financial Principles
- Fee Procedures & Processes
- Australian & International Case Studies

Introduction

MCE recommendation - ***“funding for the AER and the AEMC will be through appropriate industry levies approved by the MCE”.***

For the purposes of this consultation:

- AEMC and AER will be required to recover all of their costs through a combination of ‘fee for service’, a ‘licence fee’ or a ‘levy’ on industry participants.
- This consultation is not addressing the legal or constitutional constraints that might impact upon the choice between these approaches or their design or means of application.

Comment is sought on all aspects of the discussion paper, with emphasis on key areas such as the identification of the most economically efficient mechanisms for the cost recovery and an analysis of the administrative efficiency and practicality of these options.

Background & Objectives

Funding mechanism should seek to foster following objectives:

- Promote economic efficiency
- Promote competition within and between each energy sector
- Facilitate equity between industry participants, and between end users
- Provide transparency to the energy sector, and in particular to the stakeholders who financially support the funding mechanism
- Provide an incentive for the AEMC and AER to be financially responsible and to fulfil their legislative functions in an independent manner
- Provide incentive for energy sector participants to behave in a responsible manner within constraints provided by legislation and associated regulations, without excessive recourse to appeals mechanisms.

Background & Objectives (2)

Economic and financial principles assumed as design objectives:

- Funding mechanisms should be simple
- Financial impact of the funding mechanism should be predictable
- Promotion of economic & financial efficiency
- Promotion of transparency

Economic & Financial Principles

Discussion of the fee structure for the AEMC and AER structured as follows:

1. Identification of cost pools
2. Considering appropriate cost drivers for cost pools
3. Understanding the nature of costs
4. Assigning costs to fee components
5. Options for recovery

Economic & Financial Principles

1 - Identification of Cost Pools

- Need to define cost structure based on major rule making and regulatory activities and gathered into cost pools
- Primary cost pools used by AMEC & AER to establish cost base



- Distinction in the nature of activity -“normal” or standard activities and “extraordinary” (eg. establishment, defending legal appeal)

Feedback sought on how these extraordinary costs might be included in funding arrangements.

Economic & Financial Principles

2 – Appropriate Cost Drivers

A separate issue is the identification of cost drivers of the AEMC and AER's cost pools

- To the extent that a cost pool has a cost driver, fees structure should include component related to cost driver
- Costs associated with normal functions recovered from industry sector that benefits from that activity
- Extraordinary costs recovered via specific fee for service
- Incremental revenues factored into cost recovery


Feedback is sought on how incremental revenue sources could be incorporated with specific fee structures.

Economic & Financial Principles

3 – Understanding the Nature of Costs

The costs of the AER and the AEMC will be either:

- Variable;
- Fixed;
- Joint;
- Common; or
- Sunk



These will impact on the appropriateness of alternative cost recovery mechanisms.

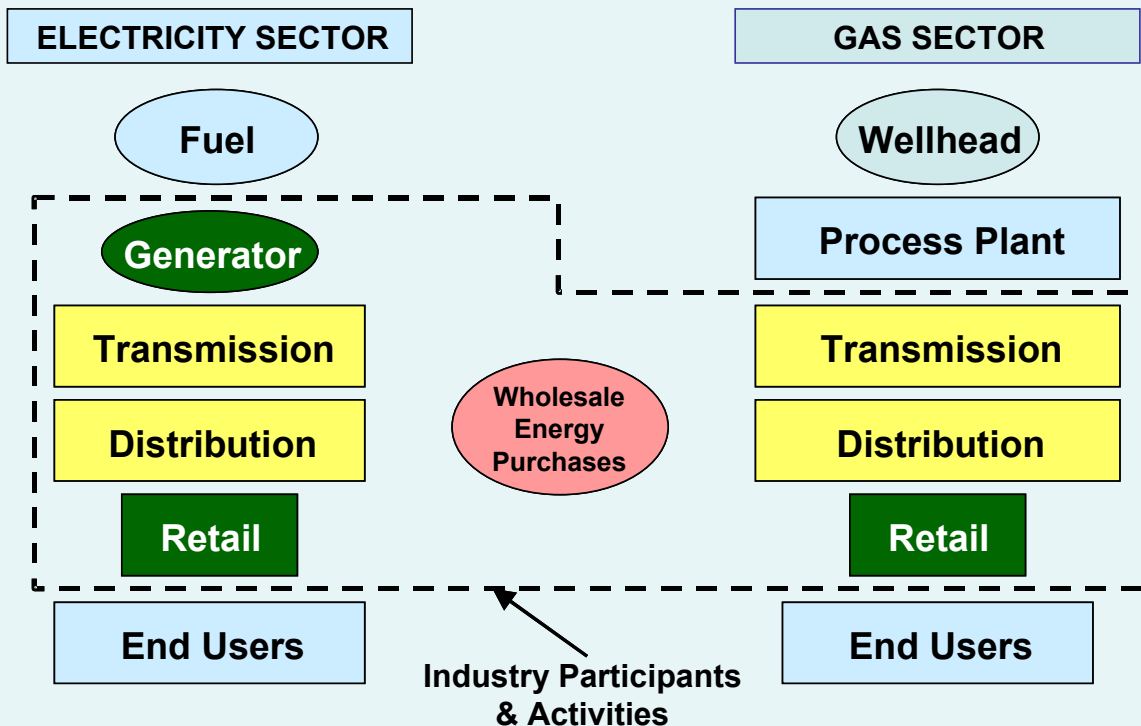
Another aspect to consider is the directness or attribution of particular costs to particular activities

Feedback is sought on the degree of detail captured and the transparency provided on the costs for efficient industry rule making and regulation.

Economic & Financial Principles

4 – Assigning Costs to Fee Components

To assist discussion, a simplified categorisation of the two competitive energy sectors under consideration has been adopted.



Ultimately, the end user pays for all efficient costs in supply chain.

Cost recovery mechanisms should provide the “least” distortion on end users ability to choose an energy type and/or supplier in an economically efficient manner.

Economic & Financial Principles

4.1 – Cost Recovery from Industry

- Economic efficiency achieved through adoption of “user pays” principles for attributable costs of costs “caused” by that entity”
- Financial efficiency achieved through the adoption of a full cost recovery mechanism
- Appear to be four general approaches for allocating costs to industry participants

Economic & Financial Principles

4.1 – Cost Recovery from Industry

Cost	Approach to Allocation
Direct, variable	User pays fee for service, based on a variable charge.
Direct, fixed costs	User pays fee for service, based on a fixed, periodic or postage stamp charge.
Joint, variable costs	To industry participant group of industry sub-sector in a manner which provides incentive for them to behave in a responsible manner to support fair competition in relevant markets, based on either a variable charge or a fixed, periodic or postage stamp charge.
Common, variable costs	To energy end users based on a variable charge which provides equity and reduces barriers to choice by end users OR allocate these costs as closely as possible to end users through an industry participant which is not competing in a market, based on a fixed, periodic or postage stamp charge.

Economic & Financial Principles

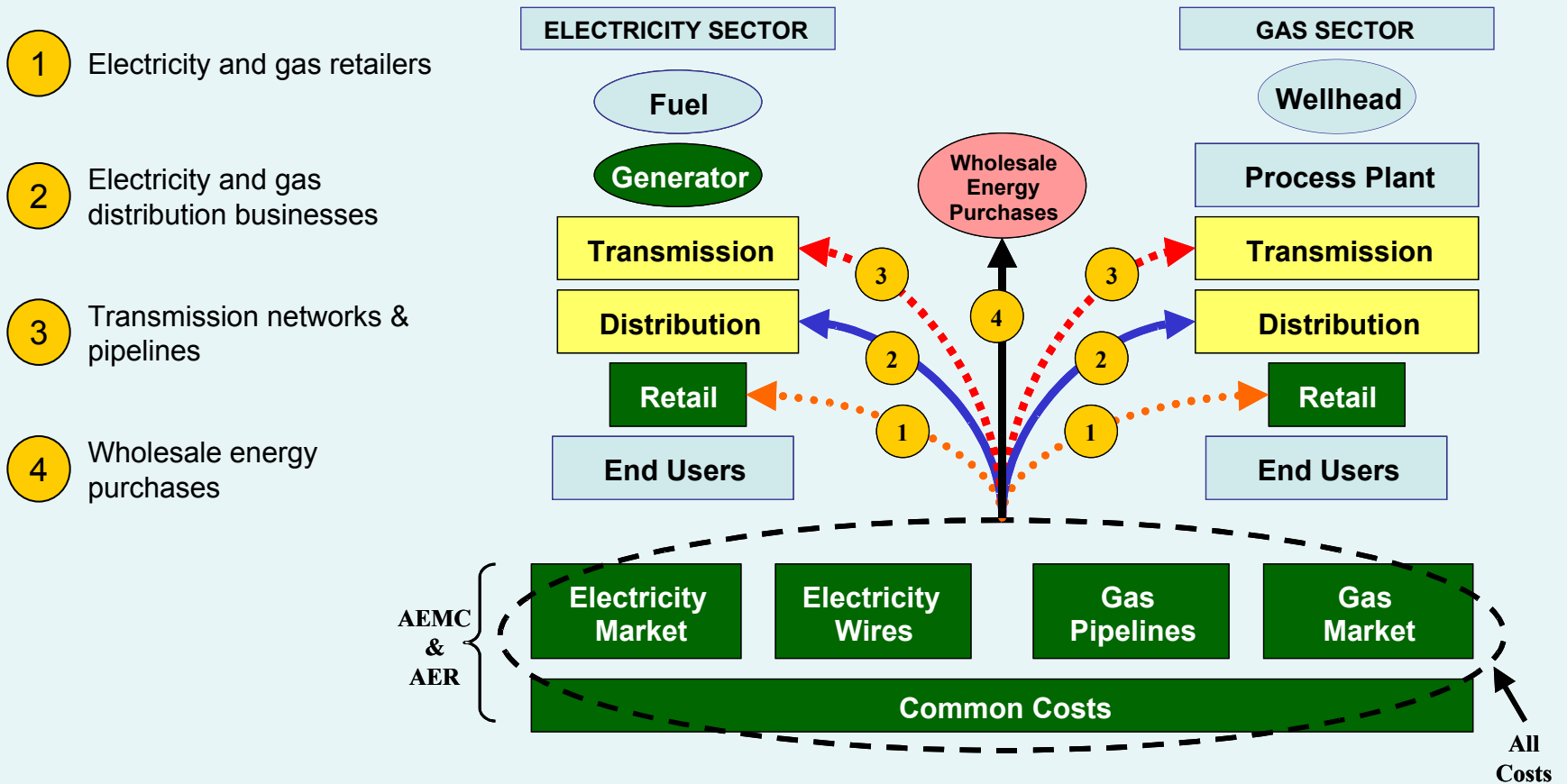
4.1 – Cost Recovery from Industry (2)

Cost allocation mechanism and charge structure used by the AEMC and/or AER could be based on a number of energy sector metrics:

- Energy throughput measured in sector specific terms eg: MW, MWh or GJ
- Thermal efficiency adjusted energy throughput which accounts for the calorific potential delivered to the end user (assuming common energy usage), eg: J
- End User numbers connected
- Number of sub-sector industry participants
- Transmission capacity reserved or used, eg: MW or GJ
- Peak load reserved or used, eg: MW or GJ
- Electricity voltage or gas pressure delivered, eg: kV or kpa
- Gross revenues (a measure of market importance)
- Net revenues (a measure of profitability and ability to pay)
- Other

Economic & Financial Principles

5 – Options for Cost Recovery



Economic & Financial Principles

5 – Options for Cost Recovery (2)

Comment is sought on allocation methodology used to attribute cost recovery between energy sectors in a competitively neutral manner.

A secondary issue which needs resolving is means of allocating sector cost recovery between industry participants and industry activities in the relevant energy sector.

The discussion paper provides an overview of the potential impacts of seeking cost recovery from different industry participants and industry activities (Sectors such as Retailers, Distribution Businesses, Transmission Businesses and on Wholesale Energy Purchases)

Comment is sought on the issues raised by having these sectors recover rule making and regulatory costs.

Fee Procedures & Processes

In developing future changes to the AEMC and AER fee structure after their initial establishment, consideration should be given to adopting a transparent review procedure, including consultation with industry participants.

A periodic consultation process (eg: 3 to 5 years) could be considered for a fee structure review procedure which might involve:

- **Liasing with the MCE**
- **Public consultation**
- **Prepare and publish initial terms of reference and issues paper**
- **Receiving submissions on the issues paper**
- **Conduct one or more public meetings to facilitate discussion on written submissions**
- **Develop recommendations for the fee structures**
- **Present a summary of consultation findings and recommendations on fee structure**
- **Incorporate feedback from the MCE and prepare final fee structure arrangements**
- **Issue final recommendation**
- **Promulgate the fee/levy**

Feedback is sought on the means and frequency of a fee structure review.

Submissions by 7 April 2004

- Email: MCEMarketReform@industry.gov.au
- Post: Industry Levy
c/- MCE Market Reform
Department of Industry, Tourism & Resources
GPO Box 9839
Canberra ACT 2601
- Facsimile: (02) 6213 7110