

MINISTERIAL COUNCIL ON ENERGY

Communiqué

Canberra, 6 February 2009

Australian, State and Territory Government Energy Ministers met in Canberra on 6 February 2009 for the 18th Meeting of the Ministerial Council on Energy (MCE). The meeting was chaired by the Hon. Martin Ferguson MP, Australian Government Minister for Resources and Energy. The Council comprises Australian, State and Territory Government Ministers and has responsibility for national policy and governance of the Australian energy market.

Key outcomes were:

- Discussion of the MCE's role in assisting energy markets to deal effectively with the implementation of the Carbon Pollution Reduction Scheme and expanded Renewable Energy Target.
- Release of the *Ministerial Council on Energy Forward Work Plan related to the Energy Market and Climate Change Policies*.
- Requesting the Australian Energy Market Commission (AEMC) to undertake a review of energy market frameworks in light of the impact on electricity supplies during the recent heat wave events. In addition, NEMMCO was requested to review opportunities to improve communications, in such events.
- Agreement to develop a work program to give effect to the Council of Australian Governments (COAG) national principles for feed-in tariffs for renewable energy.
- Recognition that the Energy Technical and Safety Leaders Group will shortly release its discussion paper on Harmonisation of Energy Supply Industry Technical and Safety Regulation for stakeholder consultation.

Recent market events

Ministers received a presentation from the National Electricity Market Management Company (NEMMCo) on recent electricity supply issues in South Australia and Victoria resulting from heat wave conditions. Ministers noted the physical constraints of electricity infrastructure during high temperatures and also emphasised the importance of communication on the energy industry's response to managing such situations.

Given the significant nature of these events, MCE agreed to request the AEMC to review energy market frameworks in light of the impact on electricity supplies of the heat wave of 29-31 January 2009.

The review will consider a range of possible reforms, including whether the level of the NEM price cap (VoLL) should be raised to ensure adequate levels of generation to reduce the risk of loss of supply during heat wave events. NEMMCO has also been requested to review communication flows and potential changes to the framework around Reserve Trader arrangements.

Climate Change

Ministers received a presentation on the Carbon Pollution Reduction Scheme (CPRS) White Paper, from the Commonwealth Department of Climate Change. Ministers also considered advice from the Australian Energy Market Commission (AEMC), the Australian Energy Regulator (AER) and NEMMCo, and a presentation from industry representatives.

Ministers recognised the implementation of the CPRS and expanded Renewable Energy Target (RET) will pose significant challenges to energy markets in Australia. As a means of informing energy market participants about MCE actions to ensure energy markets are well-positioned to deal effectively with the implementation of climate change policies, Ministers are pleased to release the *Ministerial Council on Energy Forward Work Plan related to the Energy Market and Climate Change Policies* (Attachment 1). The Work Plan includes a readiness review of prudential and related financial arrangements in the national energy markets.

Ministers agreed to establish industry consultation processes to encourage industry input and feedback on energy market issues related to climate change.

Feed-in Tariffs

The MCE noted that COAG agreed at its 29 November 2008 meeting to a set of national principles to apply to new feed-in tariff schemes for renewable energy, and to inform the reviews of existing schemes. Ministers also noted that the COAG decision requires further action by the MCE and jurisdictions to advance the fair treatment of small renewables and to promote consistency in feed-in tariff policy with previous COAG agreements. The MCE requested that officials develop a work program to give effect to the COAG principles, for consideration at the next meeting.

Review of Weighted Average Cost of Capital (WACC)

MCE noted that the AER, as an independent regulator, has released a draft review of WACC parameters and is currently considering stakeholder feedback on that draft prior to final determination of the issue.

Energy Technical and Safety Regulation

Ministers noted that the Energy Technical and Safety Leaders Group (Leaders Group), established following the MCE meeting on 13 June 2008, has developed a discussion paper on Harmonisation of Energy Supply Industry Technical and Safety Regulation.

Ministers noted that the Leaders Group intends to issue the discussion paper for stakeholder consultation. Ministers also noted that following stakeholder comment, the Leaders Group will release a draft Energy Technical and Safety Harmonisation Plan and consultation Regulatory Impact Statement. Ministers requested that the Plan be finalised for consideration at their December 2009 meeting.

The Leaders Group's discussion paper will be available on the MCE website www.mce.gov.au.

Global Carbon Capture and Storage (CCS) Institute

Ministers welcomed advice that the Global CCS Institute continues to take form, with the launch expected shortly. Founding Members will be announced at the launch, and Ministers were pleased to note that a number of countries and companies have indicated interest in becoming a Founding Member.

Attachment 1

MINISTERIAL COUNCIL ON ENERGY

Forward Work Plan The Energy Market and Climate Change Policies

The Ministerial Council on Energy (MCE) recognises the importance of implementing climate change policies for the long term benefit of Australia's society, environment and economy. To address the impacts of climate change the Australian Government has recently released papers outlining the design of the Carbon Pollution Reduction Scheme (CPRS) and an expanded Renewable Energy Target (RET).

The CPRS White Paper, released on 15 December 2008, recognised the challenges faced by energy markets in transitioning to a carbon constrained economy. Delivering low emissions outcomes will require open, national, integrated and well functioning energy markets that are able to respond to disruptions, structural change and future demand growth in an efficient and effective manner.

The MCE recognises that, to achieve the twin objectives of transitioning to a low emissions economy while maintaining long-term energy security and economic prosperity, reforms to the existing energy market frameworks may be required.

A number of current MCE reform work streams are directly relevant to ensuring the energy market effectively transitions to a low carbon economy. Ministers have also identified additional areas for further consideration. In this regard, Ministers have committed to the following key activities aimed at delivering open and well functioning energy markets:

- an assessment by the Australian Energy Market Commission (AEMC) of energy market frameworks in light of climate change policies,
- a proposal to the Council of Australian Governments that it amend the 2006 Australian Energy Market Agreement to specify that, where retail prices are regulated, energy cost increases associated with the CPRS shall be passed through to end-use customers,
- developing a National Transmission Planner, as a constituent part of the Australian Energy Market Operator, to ensure that investment in network infrastructure is nationally focussed and occurs in an efficient and timely manner,
- the reform of gas markets to accelerate the development of a reliable, competitive and secure natural gas market and to further increase the penetration of natural gas, given the increased gas use anticipated as a result of the introduction of the CPRS,
- addressing impediments to, and promoting the commercial uptake of, demand side response in the Australian market, incorporating the development of a framework to support the roll-out of smart electricity meters and noting the AEMC's review of demand side participation, and
- additional work streams to provide regular consultative forums with the supply industry and consumers, an assessment of prudential frameworks and task the AEMC to undertake a review of energy market frameworks in light of the impact on electricity supplies during the recent heat wave events.

Further detail of the MCE's current reform activities is at **Attachment A**. Further work to be undertaken by the MCE is at **Attachment B**.

Current MCE reform activities

Australian Energy Market Commission Reviews

Review of Energy Market Frameworks in light of Climate Change Policies

The Ministerial Council on Energy (MCE) has requested that the Australian Energy Market Commission (AEMC) undertake a review of energy market frameworks in light of climate change policies. The review addresses broader issues that may emerge over the medium term. In the 1st Interim Report, released 23 December 2008, the AEMC has identified a number of issues that may impact on energy markets. These include the convergence of gas and electricity markets, generation capacity investment, system operation with increased intermittent generation, investment to meet reliability standards, connection of generators to transmission networks, augmenting networks and managing congestion, retail price regulation, and financing new investment.

The MCE looks forward to receiving the AEMC final report on 30 September 2009. The MCE will appropriately consider and respond to the recommendations contained in that final report to ensure the necessary amendments are made to the energy market frameworks.

Review of Demand Side Participation

The MCE also notes and endorses the work of the AEMC in its review of demand side participation, which is expected to make detailed recommendations to MCE in the first half of 2009. The review extends previous work, for example by considering demand side participation in the context of reliability, wholesale markets and financial contracting. The MCE also notes and endorses the alignment of the review with the MCE-initiated AEMC review of energy market frameworks in light of climate change policies.

Retail pricing

In considering the interaction of the CPRS and the operation of retail markets, the broader issue of retail price regulation for energy consumers is being addressed by the MCE. The MCE recognised the importance of addressing regulatory impediments to carbon cost pass-through associated with the efficient functioning of the CPRS. To ensure a national commitment to the pass-through of carbon prices to end-use consumers, the MCE will ask that Council of Australian Governments (COAG) amend the 2006 Australian Energy Market Agreement to specify that where retail prices are regulated, energy cost increases associated with the CPRS shall be passed through to end-use customers.

Australian Energy Market Operator

The MCE is committed to the establishment of the Australian Energy Market Operator (AEMO) on 1 July 2009. The establishment of the AEMO is a key reform to the national energy market governance framework. AEMO will draw together the five different energy market operators that administer the gas and electricity markets in south eastern Australia, and operate them through a single national body. By administering Australia's gas and electricity markets (except in Western Australia and the Northern Territory) centrally, AEMO will be much better placed than the existing market operators to recognise and manage the growing interdependencies between the electricity and gas markets. The introduction of the CPRS and an expanded RET is likely to enhance these interdependencies, with increased gas-fired electricity generation as a lower emissions technology and as back-up generation to intermittent generation.

Network planning

The National Transmission Planner (NTP), as part of the AEMO, will play an important role in the energy market in the context of the introduction of the CPRS and expanded RET. The entry of new renewable generators into the grid may lead to changes in the location and mix of generation and the pattern of power flows across the transmission network. The NTP is a key measure to ensure that, in the face of these changing market conditions, investment in network infrastructure is nationally focussed and occurs in an efficient and timely manner.

The primary task of the NTP will be to publish an annual National Transmission Network Development Plan (NTNDP). Information contained within NTNDP, such as current and future congestion and transmission development strategies under a range of scenarios, should enhance the ability of the market to identify and respond to these investment issues in an economically efficient and timely fashion. Furthermore, such information should improve the ability of investors and market participants to assess transmission access and decide on where and when to invest.

Gas market development

The introduction of the CPRS is likely to place greater demands on gas as a cleaner source of energy for electricity generation and for direct industrial and residential use.

The MCE has recognised the critical importance of timely ongoing investment in Australia's gas infrastructure to meet the expected growth in gas demand, and has developed a number of measures to encourage this investment. Regulatory incentives for investment in gas infrastructure (already introduced into the National Gas Laws and National Gas Rules) include greenfields incentives, streamlined competitive tender process and the light handed regulation.

The MCE is committed to ongoing market reforms to accelerate the development of a reliable, competitive and secure natural gas market and to further increase the penetration of natural gas. National initiatives now underway to promote competition and greater transparency include the introduction and refinement of the gas Bulletin Board, the development of a gas Short Term Trading Market (STTM) and publication of a Gas Statement of Opportunities (GSOO) looking at the supply demand outlook over a ten year period. These initiatives will provide appropriate signals for new gas infrastructure investments.

Demand side response measures – Smart meters

The MCE is developing a framework to support the roll-out of smart electricity meters in Victoria and New South Wales, in locations where benefits outweigh costs. The framework will also support pilots and trials to be conducted in Queensland and Western Australia to further refine regional impacts on costs and benefits.

Smart meters will provide enabling infrastructure to allow consumers to monitor their energy use and measure their greenhouse gas emissions. Smart meters will also enable voluntary direct load control of high energy consumption appliances such as air conditioners and pool pumps to reduce stress on the power system during peak periods and reduce the need for investment in under-utilised peak-only energy infrastructure. Analysis indicates that reductions at peak times also provide an overall greenhouse gas benefit. Smart meters also offer potential business process improvements for networks and retailers.

Wind energy grid integration

The MCE developed a number of initiatives as part of the original Mandatory Renewable Energy Target. These initiatives are now in place (further details are available AEMC website). However, further work remains to better integrate wind and intermittent generation in the National Electricity Market (NEM). Areas of further work include:

- improving the Australian Energy Wind Forecasting System's forecast capability and adding functionality to forecast other renewable energy types, such as solar power,
- developing intermittent generation simulation tools for electricity system modelling and planning, and
- research and development of technologies that increase the efficient use of intermittent generation in the NEM.

Fair treatment of small renewables

The CPRS and an expanded RET are likely to result in an increased share of renewable generation in the generation mix. The MCE notes and accepts COAG's request that the MCE continue to advance fair treatment of small renewables, as announced by COAG at its 29 November 2008 meeting. The MCE has now commenced work to implement the agreement that micro renewable generation is to receive fair and reasonable value for exported energy. The MCE's work will be consistent with the COAG-agreed principle that any premium rate is to be jurisdictionally determined, transitional and considered for public funding.

In addition, the MCE is in the process of creating a new national framework for electricity distribution network planning and connections. This, in part, seeks to ensure a level playing field for the role of embedded generation, demand side response and renewable energy generation in delivering Australia's energy needs.

Retailer of Last Resort

In the unlikely event that a retailer must exit the energy market due to higher market costs related to the introduction of the CPRS and an expanded RET, a Retailer of Last Resort (RoLR) scheme will assist the customers of the exiting retailer by providing continuity of energy supply, while also being designed with the aim of the least impact on the market. MCE is committed to implementing reform to the RoLR scheme as part of the National Energy Customer Framework.

National framework for transmission reliability standards

The MCE recognises that a nationally consistent framework for transmission reliability standards will assist with investor confidence in the energy market by increasing the level of transparency and specificity of jurisdictional reliability standards. The AEMC has provided its final report recommendations to MCE for consideration. The MCE is expected to release its response to the final report recommendations in the first quarter of 2009. A consistent framework, along with other reforms, will assist with the efficient investment in generation and transmission needed to meet the government's climate change policy objectives.

Financial markets

The MCE recognises the important role that energy financial markets play in the efficient supply of energy. The wholesale electricity market is particularly volatile, and can result in potentially very large price shifts within as little as five minutes. The introduction of the CPRS and an expanded RET is likely to exacerbate this spot market volatility. Energy financial markets provide a key mechanism for managing price risks associated with this volatility efficiently.

The MCE recognises the need for a closer examination of the capacity of market participants to meet prudential arrangements under this changed policy environment.

Separation of ownership for generation and transmission

The MCE is developing provisions to separate generation and transmission assets in the national electricity market to ensure the competitiveness of the market is maintained. These provisions are particularly important with the expected increase in low-emission and renewable energy investment, brought about by the implementation of the CPRS and an expanded RET, as they will ensure new low-emission and renewable energy generation can compete effectively in the market.

Review of derogations and difference

The MCE has committed to review all remaining derogations in the national regulatory framework to ensure that, to the extent practicable and appropriate, derogations from the national framework, and other state-specific differences, are removed or harmonised.

Western Australia and Northern Territory integration

The Western Australia and Northern Territory energy markets are currently operated largely independently of the national energy market, but have the option of participating in these arrangements. The MCE recognises that the application of a consistent framework capable of delivering efficient regulatory decisions will enable an efficient pass through of costs associated with CPRS and an expanded RET.

Attachment B

Additional work streams

The current activities being undertaken for the MCE broadly address both supply and demand issues within energy markets. However, additional areas, pertinent to business operations during the implementation phase of climate change policies will need to be addressed in the future. As such, formalised consultation and feedback mechanisms will assist MCE in undertaking these work programs.

Business consultation forum

The MCE recognises that the implementation of the CPRS and an expanded RET will lead to a structural change in the energy sector. To ensure that the sector is provided with accurate information, the MCE proposes an information sharing forum. Supply and demand industry participants will receive updates from relevant Commonwealth Departments as well as the three market institutions (the Australian Energy Regulator, AEMO and AEMC) on progression in their work. Additionally, the forum is aimed at providing industry participants with the opportunity of raising concerns with the implementation of climate change policies in an MCE officials' forum.

Business readiness

Currently, there are a number of uncertainties surrounding the degree that the implementation of climate change policies will impact on the financial and energy contracting positions of NEM participants. However, the risks for market participants, and more broadly for the security and continuity of energy supply, are relatively substantial. A detailed assessment of the adequacy and readiness of NEM prudential arrangements for market participants subject to CPRS obligations would be beneficial for informing the MCE. It is proposed that MCE approach the AEMO to develop a draft terms of reference for the readiness assessment by the end of March 2009 for consideration by Officials. The assessment would have regard to related impacts in gas markets, and the proposed RET. The MCE would commission the report from AEMO for conclusion by end 2009. The CPRS readiness assessment for the energy sector will provide an indication of the severity of identified risks, an indication of the probability of risk occurrence, and will inform an MCE assessment of whether there is a need for a risk management plan.

Heatwave event of January 2009

That MCE agree that the AEMC, by a process to be determined in consultation with the MCE, will review energy market frameworks in light of the impact on electricity supplies of the extreme heat wave of 29-31 January 2009.

The review will consider a range of possible reforms, including whether the level of the NEM price cap (VoLL) should be raised to ensure adequate levels of generation to minimise risk of loss of supply in extreme events.