



Submission to the Ministerial Council of Energy

Australian Energy Market Operator Establishment – Legislative Framework Statement of Proposed Approach

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1 Introduction

Jemena Limited (Jemena) welcomes the opportunity to provide feedback to the Ministerial Council on Energy and the Implementation Steering Committee on the “AEMO Establishment – Legislative Framework: Statement of Proposed Approach”. This response is on behalf of our distribution businesses, Jemena Electricity Networks (Vic) and Jemena Gas Networks (NSW), and our gas transmission business, Jemena Pipelines (Eastern Gas Pipeline, VicHub and Queensland Gas Pipeline).

Jemena has contributed to a number of industry submissions including those from the Gas Market Company (GMC), the Australian Pipeline Industry Association (APIA) and the Energy Networks Association (ENA). Jemena supports these industry association submissions, and endorses their recommendations.

2 Executive summary

Jemena supports the national reform process in working to increase national efficiency by combining existing market operators into a single body. This promises to lower the cost of doing business nationally, through improved economies of scope and scale, resulting in lower overall costs of providing energy to the end consumer.

Achieving the promised benefits however, requires that the method of implementing the reforms must be complementary with the objectives.

Central control vs market flexibility in gas

Jemena is concerned that the proposed approach in the paper may have the unintended effect of creating a centrally controlled and facilitated market in gas. The new market could deprive the industry of opportunities to constructively innovate and deliver market based solutions to emerging issues. Many of the envisaged benefits of a national market operator can be achieved by implementing a centrally managed framework. However, this framework must recognise positive jurisdictional differences if it is to preserve the existing jurisdictional efficiencies.

Further, as the national gas market operator described in the MCE paper, AEMO would have minimal accountability and the arrangement would impose increasingly onerous obligations for participants. Such obligations would increase formality, complexity and cost in the areas of compliance, dispute resolution, and rule and procedure change.

The primacy of gas access arrangements, existing contracts and access principles

Where a Rule or Procedure conflicts with an AER approved gas network access arrangement, the access arrangement must prevail. Similarly gas transmission contracts must prevail to the extent of any inconsistency with a Rules or Procedure to maintain consistency between the service and the service offered to the shipper.

New information gathering powers for the market operator

Jemena is concerned with the MCE’s proposal that AEMO be granted broad new information gathering powers. These powers are not justified and lack appropriate safeguards.

The information gathering powers afforded to the market operator could potentially bypass good regulatory practice.

Jemena has significant concerns with the proposed use of Market Information Orders and Notices (MIOs and MINs). MIOs and MINs should be constrained in the Rules to apply only in respect of the AEMO's existing functions or powers. If any other functions are canvassed in the future, these must be subject to a Rule change .

Jemena is also concerned that AEMO's power to use and share information may not be limited. This power is unnecessary for a market operator and potentially harmful to the legitimate interest of market participants. AEMO should be constrained from using information for purposes other than the initial purpose for which the data was collected. AEMO should be obliged to protect confidential information.

Cost accountability

In order to ensure the proposed approach is optimal, accountability frameworks need to be established. In particular, there should be clear cost accountabilities for AEMO that recognise the creation of a legislated monopoly framework.

Our detailed comments on each of the regulatory design areas in the consultation paper are discussed in section 3 of this response.

3 Detailed Comments

3.1 Relationship of Rules and Procedures to Access Arrangements and Contracts

3.1.1 The primacy of gas access arrangements and existing contracts over any rule or procedure developed

Gas access arrangements and related contracts

The economic regulatory framework for gas requires owners of covered pipelines to each have an access arrangement to facilitate third party access to the network on reasonable terms. The AER's approval process provides a good level of certainty for the network operators and network users, in relation to prices, terms and conditions for access. The National Gas Law states that a network service provider should be provided with an opportunity to recover at least its efficient costs.¹

To maintain this, and to prevent unintended secondary economic regulation, it is essential that if a Rule or Procedure conflicts with an AER approved access arrangement, the access arrangement must prevail. Without this provision, the basis of access, or the nature of ancillary services provided by the network operator to facilitate market operations between network users, may be inadvertently altered. Such a change may conflict with or overturn operational or economic assumptions used to establish the costs underpinning a fair market price and terms and conditions for reference contract services.

Existing gas transmission contracts and access principles

In the case of the Jemena Pipelines, the relationship between shippers and the pipeline owner is governed by bilateral contracts. Although none of the pipelines is covered, Jemena maintains and publishes access policies for its pipelines

¹ Section 24(2) of the National Gas Law.

including standard terms and conditions that are consistent with existing contracts. As new Rules and Procedures may interfere with existing contractual rights and obligations, it is again essential that if a Rule or Procedure conflicts with an existing contract, the contract must prevail. Even in the case of new agreements, the interaction between services on a pipeline mean that any proposed Rule or Procedure must maintain consistency between new services and services offered to existing shippers.

3.1.2 The ability of the network operator or pipeline operator to recover costs of providing additional or changed market services

NSW and ACT retail gas market

In the NSW and the ACT gas jurisdictions, the network operator is currently provided with a cost recovery mechanism to recover the cost of change necessary to support wholesale and retail market changes.

The role of the network operator in NSW and the ACT encompasses supply scheduling, and custody transfer meter allocation and reconciliation to ensure that both adequate gas is brought to the network each day, and following this, liability for that gas is properly assigned amongst network users.

Given the extent to which network operators in the NSW and the ACT jurisdictions perform functions, which are provided by market operators in other jurisdictions, maintaining a network operator cost recovery mechanism similar to that afforded to market operators maintains consistency and equity. This is consistent with our comments in section 3.1.1 of this submission.

Similarly, given the central role of the network operator in the NSW and the ACT jurisdictions, the majority of market changes proposed by retailers to improve operational or financial efficiency of the retail market require the network operator to incur additional costs. Jemena believes that the existing cost recovery mechanisms should be maintained to ensure changes introduced for the benefit of the retail community are funded by retailers and not inadvertently by network operators.

The lack of a clear and timely cost recovery mechanism would also diminish the ability of the market to properly assess the cost/benefit of Rules or Procedure changes.

Given the gas wholesale and retail market in NSW and the ACT is contract carriage, the network operator performs the upstream and downstream measurement of gas and accounts for the delivery of gas on a customer by customer basis to enable the network and retail services to be measured and billed. As each network user has the freedom to negotiate a service agreement, services beyond those mandated may be agreed and charged on a commercially agreed basis. Providing a rules mechanism without cost recovery conflicts with this economic principle by providing an alternative path for network users to require services to be provided while potentially avoiding the commercial accountability they would otherwise have incurred.

Gas transmission

Similarly for Jemena's pipelines business, contracts do not generally permit a party to recover costs of varying operations or providing additional or changed services. As in the case of the Gas Bulletin Board and the NSW Gas Continuity Supply Scheme, in many cases these costs of making changes should be allocated to parties who derive the economic benefit of the changes.

3.1.3 The ability of the network operator or pipeline operator to influence rule or procedure changes to prevent the threat to safety or reliability of supply

NSW and ACT retail gas market

The network operator has an underlying responsibility to provide for the safe and reliable distribution of gas within the network, and has a perception of risk commensurate with that obligation. Jemena therefore recommends that the AEMO/AEMC be required to give consideration to the relevant network operator's opinion of the risk that a particular market change could bring to the safety and reliability of supply.

The management and operating practices of the gas network have been reviewed through multiple access arrangements and associated public consultative processes. Some of these network practices have been reflected in the GMC Retail Market Business Rules without change since the start of full retail contestability. These network practices have remained intact since. This has provided the certainty, practicality and flexibility required to serve the interests of all market participants fairly. Jemena recommend that significant weight be given to a network operators concerns regarding safety and reliability impacts in any Procedure change process.

Gas transmission

Similarly transmission pipeline owners have licence obligations that govern safe operation, often in more than one jurisdiction. In addition, contract procedures are designed to ensure the safety and reliability of supply. Where Rules affect pipelines, the AEMO/AEMC must be required to give strong consideration to the relevant pipeline owner's opinion of the risk a particular market change brings to the safety and reliability of supply.

3.2 Accountability framework

3.2.1 Explicit cost control measures required for a monopoly service provider

There should be clear cost accountabilities for AEMO that recognise the creation of a legislated monopoly framework.

The AEMO budget should be subject to independent review. AEMO should facilitate open and transparent consultation on the AEMO Statement of Corporate Intent and budget to ensure there is continuing pressure to reduce costs and adopt best practice operations. Without these measures there is a risk that the enlarged market operator may lack substantial budget discipline and that governments and regulatory bodies will use AEMO as an industry funded vehicle for continued regulatory intervention.

3.2.2 Allow existing gas jurisdictional dispute mechanisms to continue

The MCE paper states that disputes under the National Gas Rules or Procedures should be subject to a dispute resolution panel process. Such increased formality would serve to increase the cost and complexity of transactional level disputes.

Participants in NSW and the ACT gas jurisdictions have contractually agreed to resolve disputes bilaterally and following a process of their choosing. Jemena recommends this mechanism for the national energy market regime and a requirement for disputing parties to use it before invoking more formal dispute

resolution processes. This will enable small transactional level disputes to be resolved in a timely and cost effective manner, to allow mutually acceptable outcomes to be reached using cooperative mechanisms, and to minimise reliance on regulated escalation processes.

3.2.3 Handling of confidential information

Independent reviews should be conducted to ensure that AEMO's information handling practices reflect its internal information handling procedures, including its handling of confidential information. The paper recognises that there may be a perceived or real conflict of interest with the information used by various market functions that AEMO undertakes. The MCE paper suggests that the AEMO Board be responsible for the development of guidelines for the handling of this information, including consulting on the guideline.

With all the existing energy market operators merged into the one market operator there will be a more complete set of confidential energy information in one entity than ever before. There is a risk of leakage of this information from AEMO or misuse of the information between AEMO functions.

Jemena recommends that regular independent reviews are conducted of AEMO's actual information handling practices and adherence to its internal procedures in order for the market to have confidence about compliance with confidentiality provisions.

3.3 AEMO cost recovery

Jemena supports the draft proposal that there will be no cross-subsidies between gas and electricity and no cross-subsidies from other jurisdictions for functions carried out in a particular jurisdiction.

The MCE paper puts forward principles of simple fee structures and competitive neutrality between fee payers. However, Jemena queries the need for any change to existing cost allocation principles. The costs for a particular service must be apportioned to the prime beneficiaries in accordance with a meaningful allocator e.g. retail market share or number of market services requested.

3.4 Information Gathering Powers extended for Electricity and Gas

Jemena is concerned with the proposal that AEMO be granted broad new powers to issue Market Information Orders (MIOs) and Market Information Notices (MINs) in both electricity and gas. These powers are not justified and lack appropriate safeguards.

The paper states that there are two different models for information provision which may be used together:

- Detailed provision in Law or Rules for particular information – These information provisions operate today and are specific information provisions to meet a certain market need.
- General provision in Law or Rules that allow the making of other instruments that contain the detail – This model is based on the RIO and RIN (Regulatory Information Order and Notice) model established in the NEL and NGL which applies to the AER. The AEMC is using this extensive power afforded to the AER to justify proposing a similar arrangement for PIOs and PINs (Planning Information Orders and Notices) for the National Transmission Planning functions.

Justification of new powers

The MCE has not made a clear case as to why these strong powers are necessary when NEMMCO and other market operators have operated effectively without them. The paper proposes that these existing market operator powers remain and this new information power be an additional overlay. This has the potential to impose increasingly onerous obligations on participants.

These broad information powers are proposed for two reasons;

- The risk of the information provisions being incorrectly or inadvertently varied in the Rules is removed if the information provisions are established in the Law. There is a risk that the Rules could be amended to the disadvantage of key stakeholders that may not be active in the Rule change processes eg AEMO and governments on behalf of the community.
- Information provisions in the Rules cannot be accompanied by criminal offence provisions, instead they must be in the Law.

These justifications for the new powers are inadequate because:

- AEMC conducts open and transparent Rule change processes that governments and any other interested parties may contribute to;
- AEMC is bound by the market objective to protect the long term interests of consumers;
- AEMO is well versed in Rule consultation processes and is unlikely to support any Rules change that inadvertently reduces its powers to collect information for a specific market requirement;
- Industry challenged the inappropriate extension of powers for the AER when the RIO and RINs were established. There is no clear case why these powers should set a precedent for the AEMO and why the existing coverage of powers specific to the market needs are insufficient;
- The MCE paper sites no cases where necessary information was not provided to the market operator where there was a direct market need for the information to justify the need for criminal offence provisions.

Safeguards

A number of safeguards must be in place when these information gathering powers are created to restrict the use of these powers beyond the intent outlined in the paper without justification through a Rule change, restriction of the use of the information for the purpose it was collected and a dispute mechanism to ensure the legitimate interests of market participants are protected.

We recommend that the purpose for which the information is required must be demonstrated, and relevant to the AEMO's functions.

Provision of information is costly, especially with the formality the MCE has proposed. AEMO must be required to consider the cost-benefit of the request in all cases and not just in those cases relating to National Transmission Planning. Alternative means of satisfying the AEMO's underlying requirement should also be considered before a MIO or MIN is issued.

The paper makes the statement that "there does not seem to be any basis for limiting the use to which AEMO may put the Information". Jemena does not agree with this proposition. The starting position should be that information must not be used for any purpose other than the purpose for which it was provided (as

determined in the consultation process leading to the MIO or MIN being issued). This type of limitation would be consistent with the restrictions placed on gas service providers under the NGR. If it is considered necessary for AEMO to be authorised to use information for other purposes (or to be unconstrained in its use of information) then that case needs to be made.

The paper proposes that AEMO should be permitted to pass on information, including confidential information, to a wide range of bodies. The paper takes the AER's authority to disclose information under s44AAF of the Trade Practices Act as a relevant precedent. While there may be a case for AER to disclose information as authorised by s44AAF, that does not necessarily mean that AEMO should have the same or similar authority. In Jemena's view the case needs to be made out as to why AEMO should have such wide authority to disclose information in general and confidential information in particular. When coupled with the proposed wide powers to collect information and the proposed absence of constraints on using information for purposes other than the purpose for which it was given, Jemena is particularly concerned about the potential for information provided to AEMO, and confidential information in particular, to leak and potentially to be used inappropriately against market participants by other agencies in other spheres of regulation.

The information disclosure powers allow AEMO to share information with the ACCC, AER, ERA, AEMC, ombudsman and jurisdictional regulators etc. Where these other bodies require specific information to undertake activities within their charter the regulatory instruments already allow the market operators to provide the specific, relevant information for the task. There is no need for such sweeping information powers to be covertly provided via AEMO. If further specific information powers are required for these recipients that are not in place within the current market operation frameworks then these requirements should be subject to specific drafting and Rules consultation.

Under the MCE proposal, AEMO appears to have sole discretion on when they choose to use these broad information powers, the sharing of information, including confidential information and how they re-use this information for other purposes. To ensure appropriate accountability for the use of these powers, and no misuse of these powers, participants should have the opportunity to dispute the requests or inappropriate use of the information provided via the Rules dispute mechanism.

3.5 Emergency Management across Electricity and Gas

Jemena considers that industry has a wealth of knowledge to contribute to emergency management and should effectively participate and contribute in the development of any framework to manage emergencies. Jemena also consider that government intervention should be a last resort.

The paper states that an emergency management working group of officials and market operators will convene to consider the legal framework of emergencies across electricity and gas, and in multiple jurisdictions.

Jemena considers that industry is best placed to provide the relevant operational and commercial knowledge to most effectively manage, and in some cases, avoid emergencies. Any proposed emergency management process must include adequate industry representation for that reason. Jemena considers that the guiding principle for such a working group must be that the market is left to resolve the situation and government intervention should be a last resort where it is clear that the market mechanisms are unable to work.

3.6 Delineation of Gas Rules and Procedures for the wholesale/retail markets

Jemena recommends that care is taken in any reallocation of jurisdictional rules to the National Gas Rules and procedures framework to ensure that the integrity of existing market rules and processes are maintained.

3.6.1 Internal integrity of existing jurisdictional rules/procedures should be maintained

The paper suggests that Rules are more appropriate than procedures to impose substantive obligations on market participants. Rules will have a significant impact upon the economic efficiency of the market or market design, or significant financial implications for market participants. Procedures are suggested as the appropriate vehicle for the technical and procedural detail supporting the operation of the market.

Jemena recommends that care be taken in any reallocation of the existing jurisdictional rules and procedures in the gas market. Key principles must be established for allocating the existing functions between the Rules and Procedures to avoid unintended consequences of arbitrary separation. Care should also be taken to ensure the internal integrity of existing rules are not compromised.

Technical arrangements that establish metering standards, metering accuracy requirements and obligations for meter provision and meter data collection should be clearly specified in the Rules as these have significant cost impact. How these standards are maintained or the processes delivered should be placed in Procedures.

New Rules/Procedures must not alter participants market obligations. Care must be taken in the correct allocation between the Rules and Procedures to ensure that the obligations placed on market participants are not unintentionally altered in this transition and that the remaining procedural documentation is a quality, workable product for the industry to use. Jemena strongly recommends that each of the jurisdictional committees be involved in ensuring the quality of the current documentation and its workability in the new Rules/Procedures format.

Avoid scope creep in Procedures/Rules and Procedures development should not be used as an avenue for a widening of rules scope, either by the expansion of AEMO activities beyond its agreed functions or by placing additional obligations on participants beyond those specified in the Rules.

3.7 Convergence of Energy Markets

Jemena recommends that a separate workstream be considered to assess the national convergence options with significant industry representation.

After a transitional period to establish AEMO and its processes, it may be desirable to consider the national convergence of the energy markets. The method of assessing national convergence strategies should be undertaken in an open and transparent manner.

The review of national convergence options, assessing strategies, justification and assessing realistic benefits after all costs have been considered should not be confused with the development of the existing jurisdictional procedures by the relevant committees.

Energy market convergence under AEMO should be viewed as a separate stream of work undertaken by an appropriate Rules/Procedures committee with significant industry representation. The timing of any plans in this area must consider the networks ability to recover costs and the appetite for change in industry in view of the possible major initiatives eg under any electricity smart metering initiatives. Work in this area must also recognise positive jurisdictional differences and seek to preserve the existing jurisdictional efficiencies.

3.8 Gas Retail Market Procedure Change Process

3.8.1 Gas market representatives impacted by the change determine the change process

Jemena recommends that the existing jurisdictional committees be consulted for all Rules and relevant Procedure changes given their wealth of knowledge and understanding of the impacts on the jurisdictions and businesses.

The paper suggests that a single committee would be used to provide input into the rules, analyse the change proposals and provide the guidance on the level of materiality of the change and hence the change process to be used. The paper also suggests that the committee could be flexibility constituted depending on the jurisdictions impacted so that all parties may be adequately represented.

It is unclear whether it is proposed to have a single national representative committee or a representative committee with the sub committees being the existing jurisdictional committees. Jemena recommends that the individual jurisdictional committees be maintained and consulted on the relevant (Procedure or Rules) changes reflective of the differing jurisdictional rules for the following reasons:

1. to maintain centralised expertise within a jurisdiction;
2. to manage interrelationships between Rules and Procedures;
3. to avoid misunderstandings given similar terms meaning different things in different areas; and
4. to avoid “voting” of those operating on one jurisdiction on issues impacting another – i.e. for jurisdictional purposes solely.

3.8.2 Gas committee size vs. effective consultation

In relation to the committee representation and proposed consultation process, Jemena recommend;

- That committee representation be limited to those with a direct financial interest and responsibility to implement the change;
- That two rounds of consultation allow more effective open and transparent consultation; and
- That the relevant jurisdictional committee may decide whether a shorter consultation process is used.

3.8.2.1 Committee representation limited to those that implement the change

The paper recommends a committee comprising a senior AEMO employee as chair with representatives of those affected by the proposed change – 1st and 2nd tier retailers, networks, users, consumers representatives from the jurisdictions

and, the AER and AEMC with observer status. This committee would be convened to assist with managing the proposed gas retail procedures changes and providing advice on recommendations to AEMO.

The committee provides advice on the materiality of a change and the process to be utilised. Given that the procedures reflect business to business or business to market operator transactions, it is difficult to see the value of having parties sitting at the table that have no direct financial interest and are not implementing the change.

When the committee discusses the impact of various Rules changes on each of the jurisdictions and the cost to industry then there may be benefit in having the AEMC present.

Jemena is concerned that the additional representation beyond the directly impacted industry participants must not be funded by participant fees or licence fees where there is little value gained.

3.8.2.2 Effective consultation

The paper proposes the bulletin board method of consultation of 15 days or approximately 35 days consultation depending on the materiality of the change. This process appears to provide only one round of consultation. For small changes this may be reasonable, however where the changes are more complex, two rounds of consultation may provide more open and transparent consultation. Two rounds of consultation allow changes to be more fully considered and allow the changes to be analysed and improved through a wider audience. Jemena considers that this is important given the transaction complexity and the possible move to a converged set of systems/processes in the future. This would also align with the electricity procedure change processes.

3.8.3 Criteria against which to assess change proposals for gas market procedures

Jemena supports a common standard upon which to assess change proposals. The common standard needs to include consistency with the network access arrangements and the ability of the network to recover costs in addition to the criteria in the MSOR.

3.8.3.1 A common standard to assess change proposals needs to be developed

The ISC proposes that AEMO be required to assess all proposed Procedure changes in a similar manner to the Victorian MSOR – that the proposal is consistent with the gas market objective, is not unreasonably costly and is more effective than any rule it is replacing.

Jemena supports the adoption of a common standard upon which to assess changes. However, Jemena is concerned that many procedure changes are for the benefit of retailers and impose costs on network businesses.

The common standard needs to include consistency with the network access arrangements. Consistent with our comments on the access arrangements, the criteria also need to take into account the terms and conditions of the access arrangements already in place, the ability of the network business to recover the costs of unforeseen changes and any impacts the change may have on system security and safety. Where a regulator through an open consultative approach has already reviewed an access arrangement, then these procedural changes should not be inconsistent with it.

3.9 AEMO's Victorian Electricity Transmission System Functions

VENCorp functions should not be automatically institutionalised in the Rules without a detailed review and consultation. However, if this is not accepted, then we consider that the drafting of AEMO in this role should be carefully crafted to allow appropriate review and change to this arrangement at a later date.

3.9.1 Further review required before integrating the AEMO in the transmission role in the Rules

VENCorp provides certain electricity transmission planning functions in the market in Victoria. This arrangement is specific to Victoria and adds to the cost and time of any network augmentation requirements due to the uncertainty regarding which of the transmission parties to contact.

The paper proposes that AEMO undertake the VENCorp functions as a natural progression of the current arrangements. The paper is also proposing that these VENCorp functions be directly assigned to AEMO in the Rules and that as a consequence, the AEMO would not need to be a registered participant in the market.

This proposed elevating of the Victorian specific arrangements to the Rules may create a barrier to the adoption of approaches which are used in other jurisdictions. Adopting this level of centralised planning requirements in the Rules may force other jurisdictions to adopt a similar approach.

Jemena submits that the proposal to integrate VENCorp functions into the Rules without further industry review and consultation is not good practice.

3.9.2 Provide clarity of the two transmission roles in the Rules

If the ISC proposal is adopted, Jemena recommends carefully drafting the VENCorp obligations in the Rules to allow appropriate review and possible change to this arrangement at a later date. The drafting should also clarify the boundary of the two transmission roles so that it is very clear which role manages certain detailed functions.