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Streamlining the Code Change Process and
AEMC-AER-ACCC Framework for a Memorandum of Understanding
c/- MCE Market Reform
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Dear Sir

PROPOSAL TO STREAMLINE THE CODE CHANGE PROCESS

Macquarie Generation supports the overall intent of the discussion papers released by the Ministerial Council on Energy Standing Committee of Officials (SCO) on the streamlining of the Code change process and the AER-AEMC-ACCC Memorandum of Understanding (MoU). However, Macquarie Generation has concerns that the proposed arrangements, without further refinement, may not achieve a substantial improvement on existing practices. Macquarie Generation supports the introduction of the Code change model submitted by the National Generators' Forum as the long term model for initiating and reviewing Code change proposals.

The combined purpose of the two papers is to institute more effective regulatory arrangements for the energy sector. The focus of the Code change paper deals specifically with the Code process and the problem of duplication and delays that have arisen under the existing regime. The proposed MoU supports these new arrangements by outlining processes for resource sharing and information transmission (including confidentiality).

Process may not reduce duplication

The SCO has attempted to solve the problem of duplication without eliminating the ACCC role. The ACCC has at times provided an important check and balance on NECA's processes. The goal was to make authorisations less burdensome by engaging the ACCC early in the Code review process and by requiring the AEMC to assess the Code change against both the Code criteria and in light of competition and access issues notified by the ACCC. The SCO hopes that this process will reduce the likelihood that the ACCC will need to undertake its own review process, including the need to call for fresh submissions.

However, there is no guarantee that this will lead to a better outcome or indeed will prevent "duplication" of reviews. Much depends on the quality of the analysis undertaken by the AEMC (which becomes the basis for ACCC deliberations). If the AEMC does a poor job of addressing the competition concerns, then the ACCC may still feel obligated to undertake its own review before making an authorisation determination.

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The ACCC must rely on the AEMC to undertake the economic analysis that the ACCC would normally apply to an authorisation. Even with ACCC input to guide the AEMC deliberations, it is not clear that this will work effectively. The risk of the new Code change body developing narrowly cast, “engineering-based” remedies to competition issues are exacerbated under this model.

The decision criteria of the ACCC and AEMC are similar but not identical.¹ Therefore, it is not clear that the AEMC undertaking its assessment of a Code change will take into account the criteria the ACCC will need to consider in authorising such Code change. A risk is that the AEMC may reject a possible Code change on grounds that it leads to a competition detriment, whereas the ACCC may have accepted the same Code change if the Commission deems there are associated public benefits.²

The Code change process anticipates that the ACCC will provide informal advice on any matter that the AEMC should raise through its consultation process. Macquarie Generation has obtained legal advice that the ACCC cannot provide binding advice to the AEMC at this point without undertaking the full consultation process. In practice the ACCC is a reactive body, and tends to rely heavily on market inquiries to inform its deliberations. Given its inability to provide definitive advice, it is highly unlikely that the informal ACCC feedback could be relied upon by the AEMC in advance of the ACCC having undertaken its own market inquiries.

In summary, the risk of continued “duplication” is high and depends on the extent to which the AEMC assessment process effectively deals with the ACCC authorisation requirements. This in turn depends on a number of factors including:

- The lack of symmetry between prescribed criteria for assessing Code changes and the ACCC net benefits test. Note that the prescribed criteria require the AEMC to have regard for the MCE policy framework (as outlined from time to time) and the Market Objectives. However, the analytical process undertaken by the AEMC may not parallel the process that would normally be undertaken in assessing the grounds for an authorisation – which requires the identification of the public detriment (detriment to the public caused by any lessening of competition) to be weighed against possible public benefits.³

¹ The AEMC apply the prescribed criteria, whereas the ACCC apply the net benefits test as outlined in the TPA.

² In practice this may never be tested. The ACCC may never have the opportunity to review such a Code change if the AEMC has previously rejected it. The consequence of this is that socially beneficial Code changes may never be put to the ACCC due to a narrower assessment by the AEMC.

³ The *Trade Practices Act* does not define what constitutes public benefit. The Australian Competition Tribunal said: “public benefit has been, and is, given wide ambit by the Tribunal as, in the language of QCMA.... ‘anything of value to the community generally, any contribution to the aims pursued by society including as one of its principle elements (in the context of trade practices legislation) the achievement of the economic goals of efficiency and progress’. .. we bear in mind that efficiency is a concept that is usually taken to encompass allocative efficiency and dynamic efficiency” (Tribunal in *Re 7-Eleven Stores Pty Ltd* (1994) ATPR 41-357.

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- Strong doubts about the value of informal advice from the ACCC on possible competition concerns within two weeks of the Code change proposal being lodged. Macquarie Generation sees this step as a potentially irreparable flaw in the proposed process;
- Whether the ACCC accepts that the AEMC has effectively addressed all competition issues notified by the ACCC.

Finally, the inherent conservatism of the entities is likely to see the AEMC refer the Code change to the ACCC for authorisation, and for the ACCC to want to undertake its own analysis. This was the pattern of events with NECA and the ACCC. There are two reasons why this may not occur as frequently, although neither is compelling:

- It is proposed to amend the Code obligations to remove the requirement to submit Code changes to the ACCC; and
- The AEMC structure is more accountable to the jurisdictions. The jurisdictions may be able to place additional pressure on the Commissioners than was previously possible on NECA. However, this assumes that the NEM jurisdictions could reach timely agreement on such matters.

Legal advice on the authorisation process

Macquarie Generation has obtained legal advice that identifies potential legal risks for market participants if the AEMC amends the Code without ACCC authorisation. Macquarie Generation has serious concerns that another party or the ACCC could commence litigation against participants for behaviour that was consistent with the Code but for which no existing authorisation applied. The inability of the ACCC to retrospectively authorise such arrangements contributes to this uncertainty.

The Code is a body of rules that, to date, the ACCC has considered as a composite whole. Amendments to one part of the Code may impact on other related parts of the Code and potentially shift the balance of public benefits and public detriment.

Macquarie Generation believes that the SCO discussion paper is deficient in not adequately addressing this issue. The SCO must explain to market participants how it intends to manage this problem under any new arrangement. Macquarie Generation observes that the strength of the NGF proposal (discussed later) is that it can manage this problem without creating risks for any organisation.

Powers of the Ministerial Council on Energy

There must be a clearer statement of the nature and scope of the Ministerial powers of policy direction, in addition to a more complete description of the governance framework for the AEMC. The proposed arrangements identify the possible involvement by Ministers in two areas:

- It appears that the scope for Ministers to influence the Code change process is *restricted* to Category 4 (changes to protected provisions in the Code). In this case MCE sign-off is required before considering a Code change. Once the MCE sign-off has been given to consider the Code change, it is not clear whether the AEMC must bring the proposed change back to the MCE for their approval.

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- The other area where the MCE policy interests appear is where the AEMC undertakes its “market development” role (p.7). It is not clear what activities constitute “market development”. It should be noted that this ambiguity exists under the current arrangements and has been a point of considerable controversy.

The MCE Policy framework is part of the prescribed criteria, and Code changes must be assessed against these criteria. There does not appear to be any scope for the MCE to take a view on whether the AEMC has effectively applied the policy framework.

Specific comments on the code change process

- The process allows the AEMC to modify a Code change proposal. It is not clear if there is any scope for a proponent to object if it deems that the AEMC has amended the Code change proposal so as to change its original intent.
- The AEMC should not be able to propose Code changes even if it has the approval of the MCE. There is a conflict for a body that reviews Code changes having the power to propose Code changes.
- The categorisation process appears to assume that Code changes that do not involve competition issues will be relatively straightforward (category 2). It is equally possible that Code changes that do not involve competition issues are also contentious and will require full consultation (there is no apparent category for these).
- Any party may dispute the categorisation and AEMC is obliged to recategorise the Code change proposal. This provides individuals with a free option to unilaterally seek a recategorisation. Macquarie Generation suggests that a minimum of four to five participants should be necessary to force recategorisation.

Independence of the authorisation and enforcement functions

The MoU discussion paper suggests that the AER will “share” staff with the ACCC. This proposal blurs the boundaries between the bodies and appears to be inconsistent with the notion of an independent AER. Although the AER may provide input to ACCC inquiries, “sharing” of staff implies the accountabilities of specific staff are split between the organisations.

This is not a good governance model. Through the authorisation process, the ACCC effectively decides the final rules that apply in the electricity sector. In addition to the ACCC role of making the rules, its staff will have responsibility for enforcing the rules. Macquarie Generation would like to see a tighter process for ensuring that the ACCC has access to AER staff on a formal arms length basis that preserves a clear line of accountability of AER staff to the AER commissioners.

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The NGF Code change proposal is the preferred model

The National Generators' Forum has invested considerable time and resources into the development of an alternate model for managing code changes in the NEM. The proposal is detailed in the NGF response to the SCO discussion paper on streamlining the Code change process.

The NGF proposal involves the drafting of a market arrangements framework that would define the scope and intent of the procedural rules. The ACCC would authorise this document and any amendment to the market framework. This would allow some flexibility for the AEMC to amend procedural rules provided that any change was consistent with the umbrella arrangements set out in the market framework.

Macquarie Generation believes that this model offers a far superior process for amending the industry procedures while preserving the integrity of the ACCC authorisation process. The model has many advantages over the proposed arrangements:

- Removes the bulk of the duplication of review processes provided that the AEMC approves changes that are consistent with the market framework;
- Provides a single point of accountability – the ACCC would concentrate on the broader market arrangements framework and the AEMC would focus on the detailed industry procedures;
- Allows an expedited change to the market procedures without the risk of legal action for participants; and
- Allows appeals against regulatory decisions on the grounds of process and merit.

Macquarie Generation recommends that the MCE should direct the AEMC to commence the development and refinement of a Code change model consistent with the NGF proposal as a priority issue upon the commencement of the new arrangements. The MCE must require the AEMC to involve industry participants in a meaningful way in the development of the new market framework document. Industry could judge the success of the new AEMC and commissioner structure on its ability to progress this issue over the next 18 months.

The SCO's Code change proposal has the potential to create legal risks for all market participants. Macquarie Generation believes that the MCE has a duty to consult on the detail of proposed legislative arrangements in this area. Industry requires stronger guarantees that any short term change in the Code change proposal will achieve the stated aims without creating unmanageable risks for those with a legal and commercial exposure in the NEM.

Yours faithfully

Signed: G V Every-Burns

G V EVERY-BURNS
CHIEF EXECUTIVE
AND MANAGING DIRECTOR
7th April 2004