

CS

Manager – Energy Market Reform Team
National Energy Market Branch
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Dear Sir

NEM REGIONAL STRUCTURE REVIEW

Macquarie Generation has signed a joint submission with a group of market participants in response to the CRA consultation paper on the NEM regional structure released during October 2004. The Group consists of generator, retailer and TNSP companies with a substantial market presence operating across the NEM.

The Group submission supports the majority of the recommendations in the CRA report. The key elements of the CRA proposal include:

- introducing an economic test of the need for a change to the regional structure;
- regular publication of information on existing and emerging congestion in the NEM;
- fixing a time frame for conducting regional boundary reviews, announcing boundary changes and maintaining any new regional structure; and
- introducing a consistent constraint formulation throughout the NEM combined with a practical measure to limit the scope for counter price flows between regions.

The Group submission outlines a number of improvements and modifications to these CRA proposals. For example, the Group endorses the adoption of an economic test for regional boundaries based on the cost benefit framework detailed in the ACCC's regulatory test. This should remove the need for the additional arbitrary criteria in the CRA consultation paper. The Group also suggests more robust thresholds for approving boundary changes.

The CRA report introduces the concept of constraint support contracts (CSC) and constraint support pricing (CSP) and recommends its further investigation as a possible interim measure to manage significant points of intra-regional congestion. The report acknowledges, but does not discuss, the significant and difficult issues associated with developing and implementing such an arrangement.

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As noted in the Group submission, such an untested concept would require substantial and detailed development before the market could consider the proposal. The key issues are the clarification of governance arrangements and the mechanism for allocating rights under the CSC regime. Market participants will never be able to agree on an appropriate basis for making the allocation decision, as has been demonstrated by the endless debate on constraint formulation. Policy makers must ultimately decide at some point how the allocation of financial rights would be made, a process that would involve winners and losers amongst participants.

Macquarie Generation does not believe that that development of such a complex and costly mechanism is justified. There are relatively few instances of intra-regional congestion in the NEM at present and it is unlikely to create material problems under most market scenarios in the future, as observed in the CRA review. The proposal for a periodic reassessment of regional boundaries combined with existing arrangements for augmenting the transmission network should be sufficient for managing network congestion. The proposal for controlling counter price flows will limit the disruption caused by any temporary intra-regional congestion.

The Ministerial Council of Energy announced in December 2003 its intention to resolve the long running debate on the NEM regional structure. Market participants and the various industry organisations have spent the last few years and serious resources on reviews and consultancies arguing about various models for managing network congestion. The Code requirement for an annual review of regional boundaries has added to the confusion. The industry and regulatory focus on this issue far outweighs the relatively immaterial nature of the problem.

Macquarie Generation believes that the time is right for the MCE to provide unambiguous instructions to the Australian Energy Market Commission to introduce the key changes to the regional boundary review process and the management of constraints in the NEM. If there is to be any further consideration and debate of the proposed CSC/CSP regime it should be deferred until these key changes are implemented and tested and the initial regional boundary review is finalised.

Macquarie Generation believes that the Group submission, representing a broad cross section of the industry, provides a workable package of recommendations for the AEMC to develop and hopefully resolve this problematic part of the initial market design.

Yours faithfully

Signed: G V Every-Burns, 15/11/2004

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CHIEF EXECUTIVE
AND MANAGING DIRECTOR