

CS

Mr John Ryan
NE Rule Change Process
c/- MCE Market Reform
Department of Industry, Tourism and Resources
GPO Box 9839
CANBERRA ACT 2601

EMAIL: MCEMarketReform@industry.gov.au

Dear Mr Ryan

Macquarie Generation has prepared a brief response to the Ministerial Council on Energy Standing Committee of Officials' (SCO) consultation paper on the *Proposed National Electricity Rule Change Process, August 2004*.

Macquarie Generation supports the stated intent of the new arrangements to eliminate duplication in the Code change process. Under the statutory instrument model the Australian Energy Market Commission (AEMC) would be responsible for assessing, reviewing and determining rule changes in consultation with the market and other interested parties. The model should remove the delays and re-engineering of rule change proposals that have reduced the effectiveness of the existing authorisation process.

Under the current model, the ACCC authorisation of the Code provides market participants with legal immunity from contravention of the Trade Practices Act if they comply with the authorised arrangements. Macquarie Generation considers that it is essential that the statutory instrument model delivers an equivalent level of legal protection for market participants that are complying with the mandatory market rules.

Macquarie Generation has obtained independent legal advice concluding that the new model would not create any material legal risk for participants provided that the rules are appropriately drafted. This would require the Code to be rewritten in a way that makes it absolutely explicit that participants are obliged to comply with the statutory rules. The SCO must ensure that it has thoroughly examined and reviewed all parts of the existing Code to make sure that any suggestion of a consensual arrangement between participants is removed from the revised drafting. Macquarie Generation would appreciate the opportunity to review the proposed rules before they are gazetted under the NEL.

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Rule making criteria

The new arrangements depend critically on the design of effective disciplines on the operation and discretion of the rule making body. Well designed rule making criteria are a fundamental part of this process. The criteria will provide the framework for the AEMC when it carries out its net benefits test and will provide the reference point for any judicial review of the analysis that supports a rule change decision.

Macquarie Generation believes that the market objectives as currently drafted require some amendment as well as the inclusion of appropriate rule making criteria to guide the review process.

The primary market objective for the market rules focuses on the promotion of the long term interests of electricity consumers. Consumers ultimately benefit through healthy competition and prices that provide a signal for adequate new investment in generation capacity. However, the stated primary objective is open to possible misrepresentation and confusion. For example, a judicial review of an AEMC decision may take a narrow interpretation of this objective and focus on measures that reduce prices in the market.

Macquarie Generation proposes the following alternative wording of the primary objective as a way of clarifying the MCE's policy intent:

“The primary market objective of the national electricity market is to promote the long term interests of consumers of electricity:

- (a) with respect to the price, quality and reliability of electricity services,
- (b) by promoting economically efficient market operations and investment in the electricity sector.”

Macquarie Generation believes that there is a lack of clarity with some of the secondary objectives in the rule making criteria. The paper does not attempt to explain what weightings or hierarchy may be applied to the various objectives. It is not clear whether a rule change proposal has to satisfy all objectives before it can be approved. The potential also exists for a conflict between objectives, for example if a rule change proposal reduces the level of competition but still delivers net public benefits.

The new rules would benefit from the inclusion of some criteria to help define the scope of the analysis needed to support a decision to amend the rules. This may include references to the types of benefits and costs that the AEMC should take into account when conducting a review. Given the policy decision to provide for judicial review of AEMC decisions, the MCE needs to provide a framework for justifying and explaining regulatory decisions that can be tested in the courts if the review process is inadequate.

The rule making criteria would require careful drafting. The criteria should not be so prescriptive or detailed that the task of the AEMC is made unworkable. Some flexibility must be built in to the model to allow the AEMC to focus on the key issues and impacts of the rule change without having to demonstrate compliance with criteria that are not relevant to the matter under review.

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Standing to initiate rule changes

Macquarie Generation does not agree with the proposal to allow any person the right to initiate a rule change proposal. The market rules provide the framework for the conduct of a spot auction for the sale and purchase of electricity. The rules were never intended to provide a consumer protection regime or the imposition of environmental obligations. It is difficult to imagine how the rules could be amended or redesigned to achieve such outcomes without reducing economic efficiency.

Market participants bear the legal risks, financial risks and the compliance costs associated with any amendment to the market rules. Allowing any person to commence a rule change proposal adds to uncertainty in the market, even with gatekeeper arrangements to screen each proposal.

Lobby groups could use the Code change process if they failed to achieve their goals in other arenas. A similar situation occurred recently in Queensland where a group of landholders attempted to frustrate a Powerlink investment in the transmission system through the regulatory test arrangements after failing to block the proposal during the planning development phase.

Governments are ultimately responsible for implementing policies and programs that directly target consumer or environmental objectives. If a proposal from a non-market group does have merit, such groups should be able to persuade their political representatives of the case for the MCE to request that the AEMC conduct a review. Otherwise, only market participants should be able to initiate rule change proposal.

Role of the Ministerial Council on Energy

Industry participants would be concerned if the new arrangements led to increased political involvement in the design of the market arrangements. The need for the MCE to agree on a rule change proposal that it directs the AEMC to undertake should provide a safeguard for participants.

Macquarie Generation understands that the MCE intends to approve formal voting procedures, with different thresholds for agreement depending on the importance of the proposal. Macquarie Generation supports the publication of the MCE voting rules, actual voting decisions and the reasons for initiating a rule change proposal.

The consultation paper notes that the MCE may issue statements of policy principles which the AEMC must have regard to when carrying out a review. Macquarie Generation does not have a problem with this proposal provided that the policy principles are consistent with the market objectives and the rule making criteria in the NEL.

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Summary

Macquarie Generation appreciates the efforts by the SCO to address the concerns that industry has had with the delays caused by the duplication of NECA and ACCC responsibilities. The various regulatory models for reviewing and approving rule changes all have strengths and weaknesses. Macquarie Generation believes that the proposed statutory instrument model can deliver a rigorous framework for amending the market rules provided that the rules are well written, the AEMC is appropriately staffed and the rule change criteria provide some discipline over the degree of regulatory discretion.

Yours faithfully

Signed G V Every-Burns – 1/9/2004

G V EVERY-BURNS
CHIEF EXECUTIVE
AND MANAGING DIRECTOR