

# 2006–07

AER WORK PROGRAM



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# The AER

The Australian Energy Regulator (AER) is Australia's independent national energy market regulator. It commenced operation on 1 July 2005.

## Our functions

Our functions include (or will include):

- > monitoring compliance and investigating and prosecuting breaches by registered participants and other persons with the National Electricity Law, National Electricity Rules (NER) and the regulations
- > monitoring the wholesale electricity market
- > economic regulation of electricity transmission (except in Western Australia and the Northern Territory)
- > economic regulation of gas transmission, and electricity and gas distribution systems (except in Western Australia and the Northern Territory; in the Northern Territory, the AER will regulate gas distribution but not electricity distribution)
- > regulation of retail markets, to the extent determined by the Ministerial Council on Energy (MCE).

The AER also provides input and assists the Australian Competition and Consumer Commission (ACCC) with energy competition matters such as merger issues and energy authorisations.

At present, the transfer of all of the AER's functions from the ACCC and state regulators is not complete. The transfer of gas regulatory functions depends on new national gas legislation. In the interim, the AER assists the ACCC with the gas transmission regulatory functions that will ultimately be transferred to the AER. This includes approval of access arrangements, applications for approval of associate contracts, approval of annual tariff changes within an access arrangement period, and gas transmission ring-fencing compliance reporting.

On 4 November 2005 the MCE confirmed its agreement to the transfer of economic regulation of distribution networks to the national regime by 1 January 2007. Energy retail regulation (to the extent determined by the MCE) is scheduled to transfer to the AER from January 2008.

# Work program

This work program sets out the key projects and areas of focus for 2006 and 2007. It outlines general timeframes to enable stakeholders to plan for and participate in regulatory processes. More detailed project timeframes for individual projects will be published closer to the start of the project.

There are several key reforms and reviews currently being undertaken in the energy market that are relevant to much of the AER's work program and will need to be taken into account as work develops. We will keep stakeholders informed about how these reforms affect our work program and the changes we may need to make.

## Key areas of work

- > Preparing for the transfer of economic regulation of distribution networks from jurisdictional regulators to the AER.
- > Issuing network determinations for electricity and gas transmission.
- > Development of regulatory guidelines for transmission and distribution regulation.
- > Monitoring of the electricity wholesale market.
- > Reporting on the operations of the energy market.

Timelines for each of these work areas are attached (appendix A).

Over the 2006–07 period the work program of the AER will increase as we assume responsibility for economic regulation of distribution networks and prepare for the first round of regulatory resets under the new, still to be finalised, national distribution regulatory framework.

Through 2006 and 2007 the AER will be working on a range of projects to ensure the smooth transition of distribution networks from state regulation to national regulation. This will involve close liaison with state regulators, regulated businesses, user representatives and other interested parties.

To facilitate the transfer of distribution economic regulation, preparatory work and consultation on the approach to energy distribution network regulation will be undertaken before the transfer. This will involve developing distribution regulatory guidelines. We will also begin work to prepare for the transfer of retail regulation functions, once the MCE has determined the scope of these functions.

During 2006 and 2007 the AER will also continue to respond to a range of applications from industry, for example:

- > applications for pass-through
- > discount applications for transmission use of system charges
- > applications for exemption from registration as an electricity network service provider and exemption from chapter 5 of the National Electricity Rules
- > requests for waiver of ring-fencing obligations
- > arbitration of gas disputes relating to terms and conditions of access
- > overseeing competitive tender processes for new gas transmission pipelines
- > monitoring and annual approval of gas reference tariffs
- > resolving disputes about whether electricity transmission network assets satisfy the regulatory test.

There is a range of ongoing work including overseeing the alternative dispute resolution scheme under chapter 8 of the National Electricity Rules.

# Regulatory resets

## Electricity transmission resets

Each transmission network service provider (TNSP) is required to apply to the AER for its maximum allowable revenues for electricity transmission network services to be set for a minimum period of five years. The process for setting electricity transmission revenues is set out in chapter 6 of the NER. The Australian Energy Market Commission (AEMC) is currently reviewing chapter 6 of the NER and expects to have amended rules operating from January 2007.

The AER's approach to regulating TNSPs under chapter 6 is currently set out in the *Statement of principles for the regulation of transmission revenues (SRP)*. The SRP states that the TNSP is to provide a revenue cap application to the AER on 1 April in the year before the commencement of the next regulatory control period.

Queensland's TNSP, Powerlink, applied on 4 April 2006 for the AER to set its maximum allowable revenues for the period 1 July 2007 to 30 June 2012. The timeline for the Powerlink reset process is contained in appendix A.

Following completion of preparatory work, a public process for the Victorian electricity transmission revenue cap (SP AusNet and VENCORP), and the South Australian electricity transmission revenue cap (ElectraNet) will commence in quarter 1 (Victoria) and quarter 2

(South Australia) of 2007. SP AusNet's revenue cap will apply from 1 April 2008 to 31 March 2013, VENCORP's revenue cap will apply from 1 July 2008 to 30 June 2013, and ElectraNet's revenue cap will apply from 1 July 2008 to 30 June 2013.

The preparatory work starting in 2006 includes revising the information requirements for electricity transmission revenue resets and ensuring that appropriate guidelines are in place to meet statutory requirements. While the basis on which this occurs will depend on the form of the final rules issued by the AEMC, consultation will start in quarter 3 of 2006. The AER will also release a decision in quarter 3 of 2006 on the regulatory accounting methodology to be applied to electricity transmission network service providers.

Within the regulatory control period, various transmission regulatory functions are performed. TNSPs are required to submit accounting information for 2005–06 in quarter 4 of 2006, to be included in the 2005–06 transmission network service provider regulatory report. The report provides interested parties with an impartial picture of TNSPs' financial performance, revenue cap outcomes, and service standards performance under the AER's performance incentive scheme. The reports are published annually; the next report will be published in quarter 1 of 2007 or early in quarter 2 of 2007. The AER will require businesses to submit

accounting information for 2006–07 in quarter 4 of 2007, and will start work for the 2006–07 TNSP regulatory report at that time.

TNSPs are subject to requirements to ring fence the natural monopoly elements of their business from the contestable elements to promote competition in contestable activities, enable competitive access to the natural monopoly element, and ensure that there is no anti-competitive cross-subsidisation. These requirements include limiting the flow of information between the regulated and non-regulated elements of the business, and ensuring there is no discrimination in favour of an associate in a related business. TNSPs are required to report on their compliance with ring-fencing obligations in quarter 3 of 2006 and quarter 3 of 2007. TNSPs' compliance with ring-fencing obligations will be monitored on an ongoing basis and compliance may be audited.

TNSPs' compliance with the service standard arrangements in their revenue caps will be reviewed annually starting in quarter 1 of each year. Each TNSP will submit its performance report in the first quarter of 2006. The AER will assess this report and consider each TNSP's compliance with their revenue cap decisions in the second quarter of 2006. This will affect prices in the 2007–08 year, depending on whether each TNSP is rewarded or penalised for their performance.

## Gas transmission access arrangements

The ACCC is currently the regulator for gas transmission pipelines in all states and territories (except Western Australia) and for transmission and distribution pipelines in the Northern Territory. It applies the National Third Party Access Code for Natural Gas Pipeline Systems (the national gas code) to regulated transmission pipelines. Under the national gas code, the regulator is required to consider and approve access arrangements submitted by a gas transmission pipeline service provider. This process involves setting terms and conditions of access, including reference tariffs for regulated services. The process for making timely assessment decisions for proposed access arrangements and proposed revisions is set out in the *Access arrangement process guideline* released in December 2005. The guideline was prepared to advise service providers and other interested parties on processes to meet the access arrangement approval requirements of the national gas code including arrangements to conclude approvals within the specified six-month period.

The AER gas transmission work program includes assisting the ACCC in its assessment of revisions to the access arrangement for the Wallumbilla to Brisbane gas pipeline (the Roma to Brisbane pipeline owned by APT Petroleum Pipelines) for the period 2006 to 2011. This work will be finalised in the fourth quarter of 2006. The AER/ACCC will assess the revisions to the south-west Queensland pipeline access arrangement (the Ballera to Wallumbilla pipeline owned by Epic Energy Queensland). This work will be finalised in the fourth quarter of 2006.

The AER/ACCC will consider GasNet's proposed pipeline expansion for the Brooklyn to Corio loop. Before it commits funding to this project, GasNet seeks the regulator's agreement under the national gas code arrangements for providing ex ante approval of investment that is not allowed for in the current access arrangement. A decision will be released in mid-2006.

GasNet and VENCORP's access arrangements for the period 1 January 2008 to 31 December 2012 are due to be submitted for approval on 31 March 2007, setting out the policies and basic terms and conditions for third party access to the Victorian gas principal transmission system. A public process on the assessment of the revisions will start in quarter 2 of 2007 and a final decision will be released in quarter 4 of 2007.

Gas transmission businesses, like electricity TNSPs, are subject to ring-fencing obligations and are required to report on their compliance with ring-fencing obligations. Gas transmission businesses will be required to report on their compliance with those obligations in quarter 3 of 2006 and quarter 3 of 2007.

# Development of guidelines for transmission and distribution network regulation

## Electricity transmission regulatory guidelines

On 15 February 2006 the AEMC released draft rules outlining its proposed amendments to the transmission revenue regulation provisions of the National Electricity Rules. A range of guidelines will be required following the AEMC's review of chapter 6 of the National Electricity Rules. Once the rules for transmission revenue regulation are finalised, the AER will start work to ensure that appropriate regulatory guidelines are in place to meet statutory requirements for network regulation. The AEMC is also reviewing transmission pricing. The AER may be required to develop, or amend guidelines to take into account changes made following this review.

The guidelines are likely to address matters such as information requirements for revenue resets, the allocation of costs between regulated and unregulated services, and the operation of service performance target incentives. The service performance target guidelines will provide incentives for greater transmission system reliability at times when reliability is particularly valued by users, and incentives to improve and maintain the reliability of those elements of the system that are most important to determining spot prices.

Further guidelines may also address efficiency benefit sharing arrangements, the post-tax revenue setting model and the roll forward of regulatory asset values. Work will start on any new electricity transmission guidelines required by chapter 6 of the National Electricity Rules, and any changes to existing guidelines, in quarter 3 of 2006. A series of consultation documents and draft guidelines will be released over quarters 3 and 4 of 2006 in accordance with the requirements of chapter 6 of the National Electricity Rules, and final guidelines will be issued within the timeframes set out in the rules.

The AER has been working with TNSPs and NEMMCO, examining the market impact of transmission constraints. The AER will release a final decision relating to the 'Market impact transparency report' in quarter 2 of 2006 and will report regularly (through weekly reports) on the market impact of transmission constraints.

The regulatory test, promulgated under clause 5.6.5A of the National Electricity Rules, is an economic cost-benefit test used by transmission and distribution businesses in the National Electricity Market to assess network investments. As the rules governing the regulatory test are amended, the AER will if necessary revise the regulatory test to ensure that it is consistent with statutory requirements. If any changes are required as a result of the AEMC's final rules on the regulatory test, the revision process will start in quarter 4 of 2006.



## Distribution regulatory guidelines

The AER aims to develop all elements necessary to carry out distribution regulation in time to undertake the electricity distribution reviews, expected to begin in mid-2008 (with prices due 12 months later). Distribution network service providers should be provided with the necessary elements of the regulatory regime 12 months before the submission of their applications. A series of consultation documents will be released over quarters 2 to 4 of 2006 and quarters 1 to 3 of 2007.

While the elements of the distribution work program depend on the nature of the regulatory framework developed by the MCE, certain details of the framework are likely to be devolved to regulatory guidelines. It is anticipated that initial work will cover a post-tax revenue model and a roll-forward model, a cost allocation methodology, an opex incentive mechanism and information requirements.

The next stage of consultation will cover service standards, tariff setting, connection and capital contribution requirements and ring-fencing requirements.

The AER may also be required to respond to other policy reforms such as developing guidelines on the application of total factor productivity price control methods.

The National Electricity Law and rules require all network service providers to register with NEMMCO. The AER may, in accordance with guidelines issued from time to time, exempt any person or class of persons otherwise required to register with NEMMCO as a network service provider. Guidelines for exemption from the requirement to register as a network service provider were issued in July 1998. Consultation on the need for changes to the network service provider exemption guidelines will start in quarter 2 of 2006 for a period of six months.

# Market monitoring and enforcement

During 2006 and 2007 the AER will continue to publish weekly and quarterly reports on the operation of the wholesale electricity market.

In addition, reports will be published as required by various provisions in the National Electricity Rules. For example, clause 3.13.7 of the rules requires publication of a report each time the spot price exceeds \$5000/MWh in a trading interval or trading intervals. There is an ongoing work program for market monitoring of the wholesale electricity market. This includes:

- > maintaining the 'market snapshot' with up-to-date information on electricity wholesale market operations on the website
- > reporting on compliance with provisions of the National Electricity Rules where required under the rules
- > liaising with NEMMCO and industry on matters of compliance and the operation of the market
- > undertaking special investigations of market incidents and enforcement action as required.

There will be ongoing compliance reviews and audits. Several areas of the National Electricity Rules will be targeted each quarter for a compliance review and audit. Approximately 24 areas of the rules will be targeted per year.

The AER will host an international conference of market monitoring agencies responsible for market surveillance in their respective jurisdictions in quarter 3 of 2006.

Reviews of the rebidding guidelines and market monitoring reporting requirements will start in quarter 3 of 2006 and will be completed (including issuing new guidelines) in quarter 1 of 2007.

The AER will issue confidentiality guidelines for National Electricity Market (NEM) dispute resolution in quarter 2 of 2006.

# Publishing information on the energy market

As well as continuing to publish weekly and quarterly reports on the operation of the wholesale electricity market, the AER will publish a report each year on the state of the national energy market. This report will draw on information available to us through our regulatory activities and other publicly available information to provide a high level assessment of energy market arrangements in Australia.

The report will set out indicators that can be used to assess the achievement of energy market objectives, and will highlight areas that may require improvement. It will target a wide audience that includes government, industry and the broader community.

The first report (for 2005–06) will focus on the NEM and regulation of energy transmission networks, but will also cover distribution and retail issues. The coverage of distribution and retail will expand in subsequent reports as regulatory responsibilities in those areas are transferred to the AER. Similarly, while the first report will include gas market issues, this area will be expanded in subsequent editions.

# Other work

The AER provides advice and assistance on the operation of the regulatory framework to energy market participants and other interested parties. This includes engaging with applicants before the start of a regulatory process such as a revenue/price reset or an application for authorisation under the *Trade Practices Act 1974*.

During 2006 and 2007 the AER will continue to assist the ACCC on competition and fair trading matters in the energy sector. This includes assistance in the review of gas market rules as part of the ACCC's authorisation function.

The AER will assist the ACCC in reviewing interim authorisations that currently apply to joint marketing arrangements of gas producers in the Cooper Basin. It is expected that the ACCC will start a review of these interim authorisations, with a view to withdrawing the interim authorisations or granting substantive authorisation.



# Appendix

## Network access regulation

Project	Commencement	Finish
<b>Powerlink electricity transmission revenue cap determination for the period 1 July 2007 to 30 June 2012</b>		
Application submitted	quarter 2, 2006	
Public forum on Powerlink application	quarter 2, 2006	
Close of submissions on application	quarter 2, 2006	
Draft decision	quarter 3, 2006	
Final decision		quarter 4, 2006
<b>Wallumbilla to Brisbane pipeline (Roma to Brisbane pipeline)—APT Petroleum Pipelines—transmission pipeline access arrangement for the period 28 July 2006 to 30 June 2011</b>		
Lodgment (proposed revised access arrangement submitted, assessment for completeness)	quarter 1, 2006	
Submissions	quarter 2, 2006	
Draft decision	quarter 2, 2006	
Submissions	quarter 3, 2006	
Final decision		quarter 4, 2006
<b>GasNet Corio Loop expansion—application under s. 8.21 of the national gas code</b>		
Application submitted	quarter 4, 2005	
Request for submissions	quarter 1, 2006	
Close of submissions on application	quarter 1, 2006	
Draft decision	quarter 2, 2006	
Final decision		mid-2006
<b>South-west Qld transmission pipeline access arrangement</b>		
Lodgment (proposed revised access arrangement submitted, assessment for completeness)	quarter 3, 2006	
Submissions	quarter 3, 2006	
Draft decision	quarter 4, 2006	
Submissions	quarter 4, 2006	
Final decision		quarter 4, 2006

Project	Commencement	Finish
<b>Victorian (GasNet, VENCORP) gas transmission access arrangements</b>		
Lodgment (proposed revised access arrangement submitted, assessment for completeness)	quarter 2, 2007	
Submissions	quarter 2, 2007	
Draft decision	quarter 3, 2007	
Submissions	quarter 3, 2007	
Final decision		quarter 4, 2007
<b>ElectraNet electricity transmission revenue cap determination</b>		
Application submitted	quarter 2, 2007	
Close of submissions on application	quarter 2, 2007	
Draft decision	quarter 3, 2007	
Public forum on draft decision	quarter 4, 2007	
Final decision		quarter 2, 2008
<b>Victorian (SP AusNet, VENCORP) electricity transmission revenue cap determination</b>		
Applications submitted	quarter 1, 2007	
Close of submissions on applications	quarter 2, 2007	
Draft decision	quarter 3, 2007	
Public forum on draft decision	quarter 4, 2007	
Final decision		quarter 1, 2008

## Development of guidelines for transmission and distribution network regulation

Project	Commencement	Finish
Development of transmission guidelines required by chapter 6 of the National Electricity Rules		
Issues paper, release of proposed guidelines and invitation for submissions	quarter 3, 2006	
Close of submissions	quarter 4, 2006	
Final decision: issue guidelines		Within timelines required by the National Electricity Rules

### Distribution network regulation guidelines

The AER will consult on a range of issues between March 2006 and July 2007. Stage 1 consists of a scoping paper which will set out the AER's approach to developing the distribution network regulation guidelines. While the chronological order of the consultation may change subject to stakeholder feedback on the scoping paper, it is currently envisaged that stage 2 will consist of consultation on a post-tax revenue model, roll-forward model, cost allocation methodology, operating expenditure incentive carry-over mechanism and information requirements. It is currently envisaged that stage 3 will consist of consultation on tariff setting, connection and capital contribution requirements, service standards and ring-fencing requirements.

Stage 1—release scoping paper	quarter 1, 2006	
Submissions on scoping paper	quarter 2, 2006	
Final decision clarifying AER's approach to developing the guidelines		quarter 2, 2006
Stage 2—release discussion paper	quarter 3, 2006	
Draft decision	quarter 1, 2007	
Final decision		mid-2007
Stage 3—release discussion paper	quarter 1, 2007	
Draft decision	mid-2007	
Final decision		quarter 1, 2008



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## Market monitoring and enforcement

Project	Commencement	Finish
Review rebidding guidelines under clause 3.8.22 of the National Electricity Rules and market monitoring reporting requirements under clause 8.7.2 of the National Electricity Rules		
Commence consultation—give notice in accordance with the 'Rules consultation process' inviting written submissions	quarter 3, 2006	
Consider submissions and hold meetings with persons being consulted	quarter 4, 2006	
Publish draft report	quarter 4, 2006	
Receive submissions on draft report and consider submissions	quarter 1, 2007	
Publish final report		quarter 1, 2007
The AER will conduct ongoing compliance reviews and audits of a range of provisions of the National Electricity Rules, with reviews of selected provisions each quarter		
Ongoing—quarterly basis		
Publish reports as required by the National Electricity Rules		
Ongoing		

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## Publishing information on the energy market

Annual state of the market report 2005–06		
quarter 3, 2006		
Annual state of the market report 2006–2007		
quarter 3, 2007		

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