




Hon Bill Johnston MLA
Minister for Mines and Petroleum; Energy; Industrial Relations;

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Dear Ms Cusworth

AUSTRALIAN ENERGY MARKET OPERATOR FIFTH ALLOWABLE REVENUE PROPOSAL – 2019-20 TO 2021-22 PERIOD

I refer to the Economic Regulation Authority's (ERA) Issues Paper released on 22 March 2019 on the Australian Energy Market Operator's (AEMO) proposal for its fifth allowable revenue (AR5) period (2019-20 to 2021-22).

As noted in the ERA's Issues Paper, changes were made to the Wholesale Electricity Market (WEM) Rules on 29 June 2018 to confer additional functions on AEMO to prepare for and facilitate the implementation of WEM and constrained network access reforms. These changes recognise that, in its dual role as the Market Operator and System Manager, AEMO possesses unique expertise required to assess the future needs of the power system, as well as to co-design and operationalise solutions through changes to its systems, the WEM Rules, and regulatory instruments.

In my 13 March 2019 letter to Ms Audrey Zibelman, Managing Director and Chief Executive Officer of AEMO, I clearly articulated my expectations regarding the scope and detail of the reforms requiring the assistance of AEMO. It is my expectation that this letter, which was attached to AEMO's AR5 submission to the ERA, provides adequate context to inform the ERA's consideration of AEMO's proposal.

In its 7 December 2018 response to AEMO's last allowable revenue submission, the ERA put forward the view that the scope of the WEM and constrained network access reforms is largely the same as those pursued by the previous Government under the then Electricity Market Review. This view should be reconsidered for three important reasons:

- the role of AEMO in progressing the current suite of reforms is more substantial than was the case with the Electricity Market Review. AEMO has been engaged earlier in the process of regulatory and market co-design to ensure improved outcomes when compared with the previous process where AEMO was mainly engaged in regards to implementation;
- the objectives of the Electricity Market Review included a transition to the national framework for electricity network regulation. This method of implementing constrained network access and other market reforms is not supported by the McGowan Government, resulting in the need for policy and regulatory design that was not contemplated under the Electricity Market Review; and

- given the time that has elapsed since the Electricity Market Review, the scope of the WEM and constrained access reforms now also need to address aspects of the rapidly emerging risks to system security from the transition to more renewable and distributed generation in the South West Interconnected System (SWIS). As the System Manager, AEMO has an essential role to play in helping to define the system security needs of the SWIS into the future.

These differences in approach, and the consequential differences in resource requirements and project scopes, should be recognised in the ERA's determination of AEMO's allowable revenue for the AR5 period.

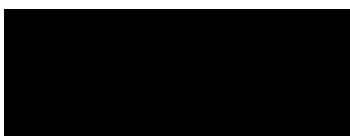
In its Issues Paper, the ERA has asked whether, given aspects of market design are yet to be determined, it would be more appropriate for AEMO to receive funding approval for a period shorter than the full AR5 period. I acknowledge that many aspects of future market and regulatory design are not yet finalised and will be determined over the next 12 months. However, many of the costs to be incurred by AEMO in implementing new market systems and co-designing improvements to regulatory frameworks will remain unchanged, regardless of the specific details of the market and policy settings adopted. Additionally, failure to provide funding certainty to AEMO over a multi-year period can only detract from its ability to plan for WEM and constrained network access reform as required under the WEM Rules and may ultimately increase the costs of AEMO's work program.

The SWIS is changing rapidly as the large-scale generation mix changes, with intermittent renewable generators making up an increasing share. At the same time, households and businesses are producing more of their own electricity and adopting new and more efficient technologies. Battery storage and electric vehicles will drive further, radical changes to the way the power system operates.

These changes create exciting opportunities to reduce greenhouse gas emissions and help customers control costs. However, these changes are not without their challenges. Our existing regulatory and market framework will, in many cases, be inadequate of the future task of maintaining power system security and reliability at the same time as efficiently delivering the electricity services required to power our communities and the economy. Modernisation of our WEM and network access arrangements, as part of these reforms, is essential to maintain a secure, reliable, affordable and lower emissions electricity supply for customers in the SWIS.

Given its dual identity of Market Operator and System Manager, AEMO's role in assisting the Government in the transformation of the electricity sector is clear. I encourage the ERA to consider this in the context of AEMO's AR5 funding proposal.

Yours sincerely



Hon Bill Johnston MLA
Minister for Mines and Petroleum; Energy; Industrial Relations

15 APR 2019