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STRUCTURE OF AEMO PARTICIPANT FEES

Dear Ms Chui

Following your email of 17 February 2016 and our subsequent discussions I am responding to the questions that you asked regarding advice provided by Allen Consulting Group in 2005 and 2010. (Allen Consulting Group is a predecessor company to ACIL Allen Consulting.) You asked me to review this advice given that AEMO must now have regard to the National Electricity Objective in its determination of participant fees.

The questions you asked are

- Can ACIL Allen please review the 2005 advice and advise whether, in light of the inserted new principle, ACIL Allen would consider that its 2005 remains consistent with the existing rules and contemporary economic approaches?
- After reviewing its 2005 advice and the rule change, recognising that the 2010 letter was written after the rule change, would ACIL Allen, on reflection of the above matters, see a need to alter its position on the 2010 letter?

National Electricity Objective

The National Electricity Objective, set out in the National Electricity Law, is to

"promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to -

- (a) price, quality, safety, reliability and security of supply of electricity; and
- (b) the reliability, safety and security of the national electricity system".

2005 Report and Advice

Our December 2005 report to NEMMCO provided a summary of the economic issues associated with the determination of Participant fees for Registered Participants. In this analysis, we had regard to a number of issues including the relevant criteria identified in the National Electricity Law and the National Electricity Rules, the application of economic objectives, as well as submissions that interested parties made in response to NEMMCO's Issues Paper on the Structure of Participant Fees.

In our report, as set out in Chapter 2, page 3, we made specific reference to the NEO, and noted that according to the second reading speech of the *National Electricity (South Australian) (New National Electricity Law) Amendment Bill*, the NEM objective is an economic concept and should

be interpreted as such. In chapter 3 of our report, we discussed economic principles and their application to a structure of participant fees, with a particular focus on economic efficiency. Chapter 4 of the report focused on the design of a participant fee structure, in the light of the previous chapter's discussion: who (which classes of participants) should pay fees, what fees should be levied, and how the fees should be divided among classes of participants.

Thus, although the NEM rules at the time of our 2005 report did not say that NEMMCO should have regard to the NEO in its determination of participation fees, our report and recommendations did have regard to the NEO. In a sense, our report anticipated the subsequent rule change.

Therefore, our 2005 advice **remains consistent with the existing rules**. Furthermore, in my opinion, it remains **consistent with contemporary economic approaches**. While economic thinking on these matters is always evolving, there have been no developments in recent years that I am aware of that would cause us to fundamentally change our advice.

2010 Letter and Advice

In December 2010 my then colleague Richard Scheelings wrote to Mr Jack Fitcher on the matter of the allocation of the 'unallocated' category of costs within AEMO's general budget.

Dr Scheelings noted that in our 2005 Report, we said that since the National Electricity Rules were silent on how to allocate unallocated costs, our advice, based on principles of economic efficiency, as set out in the NEO, was that unallocated costs should be levied on Market Customers.

Dr Scheelings further advised on an issue that arose at the time, which was whether our 2005 advice on the allocation of unallocated costs in NSW still applied given the regulation of retail prices by IPART. He advised that this regulation did not change our previous conclusions and recommendations.

A key component of Dr Scheelings' advice was that "unallocated costs are to be apportioned according to the principles of economic efficiency, consistent with the National Electricity Objective."

Accordingly, in answer to your second question, we do not see a need to change the advice provided in the 2010 letter.

Yours sincerely



Jerome Fahrer
Director