Quarterly Compliance Report:

National Electricity and Gas Laws

April – June 2014

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AUSTRALIAN ENERGY REGULATOR

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Executive summary

The purpose of the Quarterly Compliance Report **(QCR)** is to outline the Australian Energy Regulator's **(AER)** compliance monitoring and enforcement activity under the National Electricity Law **(Electricity Law)** and the National Gas Law **(Gas Law)**–including the rules and regulations which sit under those laws. This QCR covers the period 1 April to 30 June 2014 **(the June 2014 quarter).**

During the quarter, the AER undertook enforcement action against two participants for allegedly failing to comply with the requirements of the National Electricity Rules **(Electricity Rules)**. This includes:

- instituting proceedings against Snow Hydro Limited **(Snowy Hydro)** for an alleged failure to comply with the Australian Energy Market Operator's **(AEMO)** dispatch instructions (section 2.2)
- issuing an infringement notice to Lumo Energy Pty Ltd **(Lumo Energy)** for allegedly enabling unauthorised access to AEMO's market systems (section 2.3).

Compliance activity regarding the security of AEMO's market systems extended beyond Lumo Energy in the June 2014 quarter. AEMO self-reported to the AER that it breached s 91G of the Gas Law by disclosing confidential information from its markets systems to the wrong recipient (section 1.3). We also instigated a targeted review of participant compliance with the market system security requirements of the Electricity Rules (section 2.4).

We continued to respond to no action letter requests this quarter, including a no action request from AEMO regarding inconsistencies between its Meter Churn Procedures and the metering requirements of the Electricity Rules (section 2.5).

A technical audit of the electricity transmission network business, ElectraNet, was also completed by the AER. The audit focussed on the requirement to institute a compliance program for its protection and control systems. The outcomes of this audit, including the remedial actions proposed by the business to improve its technical compliance program, are included in this report (section 2.6.1).

In relation to the wholesale gas markets, the AER continued to refine its compliance monitoring framework for the Wallumbilla Gas Supply Hub **(GSH)**. In particular, we worked with AEMO to ensure its reporting arrangements provided the AER with the necessary information to monitor market conduct, particularly price manipulation (chapter 1). We also engaged with industry to clarify our approach regarding the provision of capacity data in the Short Term Trading Market **(STTM)** (section 1.4).

Finally, this QCR provides the AER's response to the opening of the Elizabeth zone valve in the South Australian gas distribution network (section 1.4) and AEMO's administered ex post pricing in the Adelaide and Sydney hubs of the STTM between 1 and 3 June.

Background

The AER is responsible for monitoring compliance and enforcement under legislation and rules governing Australia's wholesale energy markets, including those applying to Network Service Providers. Section 15 of the Electricity Law and section 27 of the Gas Law set out our functions and powers, which include:

- monitoring compliance by energy industry participants[1] and other persons
- investigating breaches, or possible breaches, of provisions of the legislative instruments under our jurisdiction.

Consistent with our statement of approach,[2] we aim to promote high levels of compliance, and seek to build a culture of compliance in the energy industry. A culture of compliance will:

- reduce the risk of industry participants breaching their regulatory obligations
- assist in ensuring industry participants can engage confidently in efficient energy markets.

As part of this process, we undertake a continuous compliance risk assessment of the Electricity and Gas Rules to identify appropriate focus areas and monitoring/compliance mechanisms. These mechanisms include our strategic compliance projects, audits, the imposition of reporting requirements, market monitoring, and targeted compliance reviews.[3]

In selecting the areas for review, we adopt the following principles:

- consideration of risk (the greater the risk, the higher the priority)
- a commitment to ensuring that both systemic issues and those with the potential for isolated but significant impact are addressed.

In carrying out our monitoring functions, we aim for:

- cost effectiveness for energy industry participants and the AER
- transparency (subject to confidentiality requirements).

While most obligations under the Electricity and Gas Rules do not require registered participants to establish specific compliance programs, we take into account a participant's compliance framework when determining our response to potential breaches. In assessing compliance culture, we consider whether compliance programs and processes are effectively applied, up-to-date and tested regularly.

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1 Entities registered by AEMO under Chapter 2 of the Electricity Rules or in accordance with Part 15A of the National Gas Rules.

2 In April 2014 the AER released a combined Enforcement and Compliance Statement of Approach covering our functions under the Gas Law, Electricity Law and National Energy Retail Law. The document reflects the consistent approach taken by the AER to enforcing the energy laws across all markets.

3 Provisions of the Gas Rules and Electricity Rules that have been targeted for review in previous quarters are listed in Appendix C.

1 Gas

We are responsible for monitoring, investigating and enforcing compliance with the Gas Law and Rules, including but not limited to, the STTM, the Victorian gas market, the Gas Supply Hub and the Bulletin Board.

This part of the report provides an update on investigations, compliance matters and projects in the gas markets.

Gas Supply Hub

We noted in the previous QCR that a new upstream GSH at Wallumbilla, Queensland, commenced on 20 March 2014. During this quarter, we monitored market activity at the GSH and continued to refine our monitoring framework to ensure we are receiving the necessary information to ascertain compliance levels, particularly in relation to the market conduct rules.

Under the Gas Rules, the AER is responsible for monitoring GSH members' compliance with rights and obligations specified in the Gas Rules, including market conduct rules. The market conduct rules seek to protect the integrity of the market by prohibiting members from a number of activities such as manipulating prices and acting fraudulently. The Gas Rules also contain obligations in relation to submitting orders, the exchange of information and the performance of contracts. The market conduct rules are classified as both civil penalty provisions and conduct provisions under the National Gas Regulations.

In the GSH, there are four spot and forward trading products available to trade including balance-of-day, day ahead, daily and weekly products. While still very early days, the majority of trades so far have been for daily and day-ahead products (each around 40 per cent of volume traded). There have been 18 weekly products traded totalling 371 TJ and almost twice the number of balance of day trades totalling just over 64 TJ. Prices have ranged between $1.40/GJ and $4.30/GJ, with prices having decreased since market commencement.[4]

[4] As at 25 July, there had been 274 trades and the volume weighted average price was $2.52.

Figure 1.1 Volume traded and prices since market start

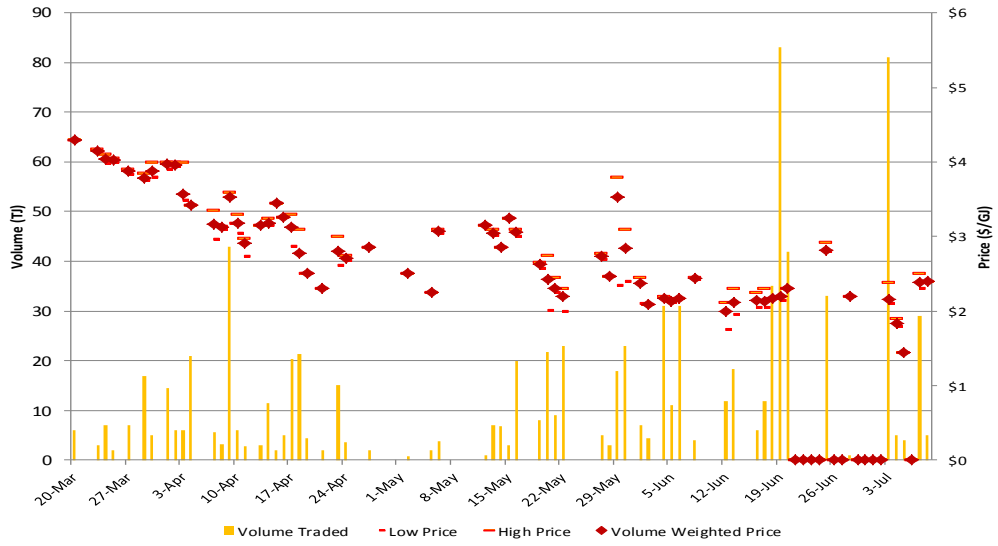
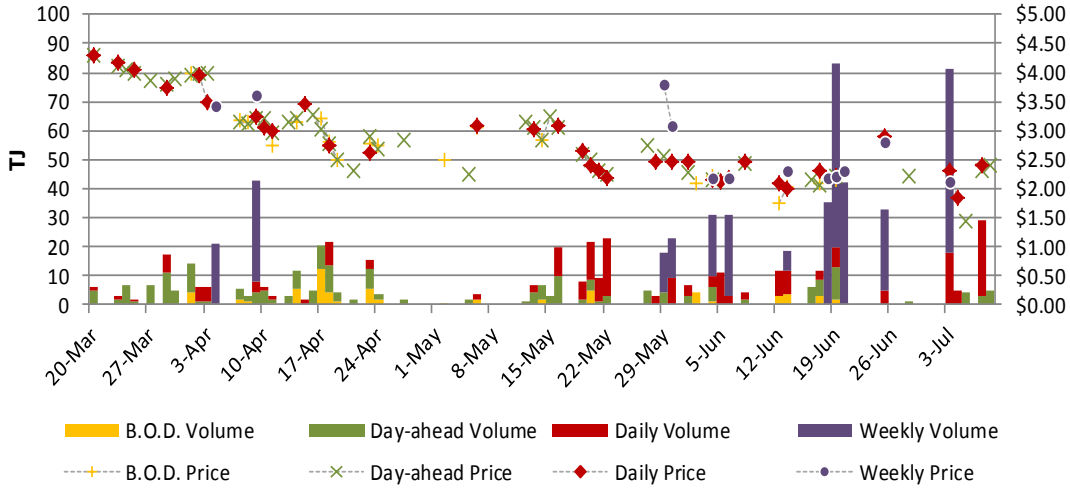


Figure 1.2 Volume traded and prices since market start by product type



We have begun monitoring delivery variations at the GSH as we flagged with industry prior to the market commencing. The market conduct rules require trading participants to trade on the basis of gas they intend to physically deliver or receive at the GSH. To date there have been no delivery variations reported to AEMO.[5] We will be consulting further to understand whether these trades accurately reflect that gas is being delivered and received.

The AER has also been working with AEMO to refine our monitoring framework of the GSH to ensure we receive the necessary information to ascertain compliance levels in relation to the market conduct rules. This has involved seeking improved information from AEMO on orders submitted in the GSH, particularly in relation to orders which are amended or cancelled by trading participants. We are also developing internal guidance on price manipulation in the GSH to assist in identifying market behaviour that may constitute price manipulation.

5 Clause 15.3 of the Exchange Agreement provides that AEMO will assume that the delivery quantity was made available for delivery and accepted by the receiving participant, unless otherwise notified in accordance with clause 15.2.

In the coming months, we intend to expand the scope of our public reporting arrangements on the GSH. We plan to build on our existing weekly reports, by including more data and analysis regarding the GSH and publishing longer term supply hub information in the industry statistics section on our website.

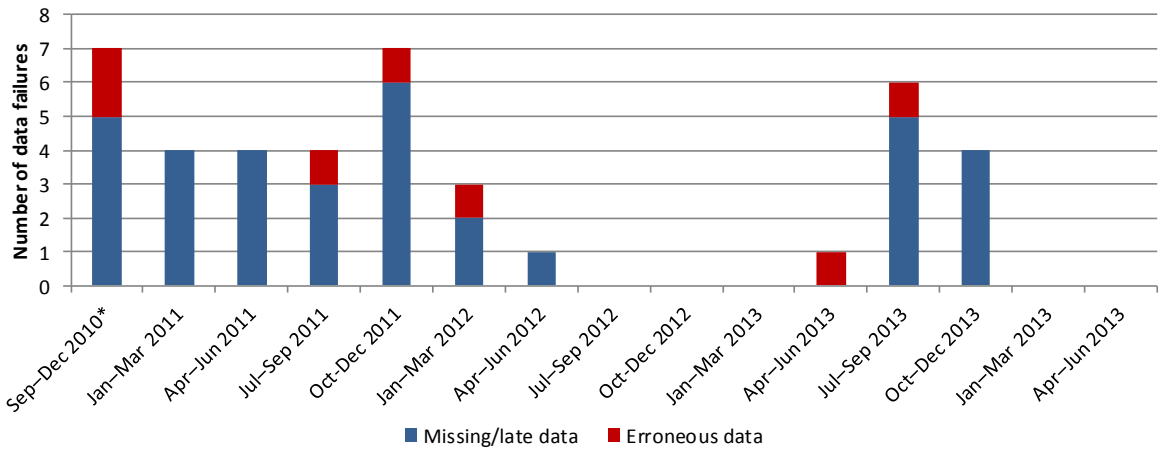
Short Term Trading Market

Part 20 of the Gas Rules sets out participants' responsibilities within the STTM, which encompasses three gas trading hubs: Adelaide, Sydney and Brisbane. The rules outline how wholesale gas is traded and include requirements for pipeline operators to submit pipeline capacity and allocation (gas flow) data.

1.1 Capacity and allocation data quality

This quarter we continued to monitor the quality and timeliness of STTM data. Figure 2.1 below illustrates the performance of STTM participants in submitting capacity and allocation data from the start of the STTM to June 2014. Data failures are categorised as relating to either 'missing/late' or 'erroneous' data. There were no errors identified this quarter.

Figure 1.3 Data failures since STTM commencement



* September 2010 has been grouped with the December 2010 quarter. Therefore, this data point represents four months.

1.2 AEMO – Administered pricing 1 to 3 June

An administered ex post price state is triggered when ex post prices cannot be published within the required timeframe.[6] When this state occurs, the administered price is set at the ex ante market price.

On gas days 1 to 3 June 2014, AEMO could not publish ex post prices under rule 426 of the Gas Rules within the required timeframes. As a result, AEMO applied an administered ex post price in accordance with clause 429 of the Gas Rules (the June event). The ex post prices are set out below in table 1.1.

[6] Clause 426(1) of the National Gas Rules requires the ex post price to be made available to trading participants 5.5hours after the start of each gas day – subject to rule 426(1A).

Table 1.1 Prices with and without administration: June 1 to 3 (Sydney and Adelaide)

	Ex post price Administered (Sydney)	Ex post price Non-admin (Sydney)	Ex post price Administered (Adelaide)	Ex post price Non-admin (Adelaide)
June 1	$3.8681	$4.0488	$3.7880	$3.7800
June 2	$3.8681	$4.0488	$3.7780	$3.7780
June 3	$3.7988	$3.7988	$3.8788	$3.8788

AEMO has reported that the event was due to issues in AEMO's market systems and how MOS allocations were being validated following the introduction of new MOS arrangements. AEMO has engaged Pricewaterhouse Coopers to conduct an end-to-end investigation of these events in order to determine root cause(s).

AEMO has found that the impact of the event was non-material having considered prices, settlement differences and effects on prudential requirements. The effect on ex post prices from administration on the market is highlighted in figure 1.4 above - the non-administered price is the price which would have applied if facility operator data had been used by AEMO on the day. AEMO reports that the small or zero differentials between the two sets of prices (administered and non-administered) for each hub on each day resulted in minimal impacts on settlement outcomes for participants. With the biggest impact being that one participant was worse off by just under $4000.

Events such as this are likely to impact on consumer and participants' confidence in the integrity of market outcomes, a strategic priority of the AER's. Accordingly we will focus our efforts to ensure AEMO take the necessary steps to mitigate the risk of a similar event occurring in future.

1.3 AEMO – Disclosure of confidential information

The Gas Law prohibits AEMO from disclosing protected information to unauthorised recipients.[7] This includes information given to AEMO in confidence or in connection with the performance of its statutory functions and classified under the Rules, the Procedures or the Regulations as confidential information.

In June, AEMO advised the AER that it had inadvertently disclosed protected information to the wrong registered participant in April 2014. The information included Delivery Point Identifier (DPI) numbers, with the associated retailer and distributor identified against each DPI. The list did not include customer details. The recipient of this information has confirmed to AEMO the data was not used and subsequently destroyed.

Since the wrongful disclosure of protected information by AEMO in April 2014, AEMO has implemented remedial actions to prevent a reoccurrence of this type of breach. This includes implementing a new process to validate data requests from registered participants.

We note this is the second time AEMO has disclosed protected information to unauthorised recipients this year. In February, AEMO provided a list of delivery point information from a NSW/ACT network operator to the wrong recipient.[8] In response to this error, AEMO implemented a number of remedial

[7] Section 91G of the National Gas Law.
[8] The information, which was provided in a CD to the wrong recipient, was subsequently destroyed.

actions including initiating a process to automate the delivery of confidential data to market participants and the introduction of file encryption and password protection measures.[9]

AEMO has committed to providing a detailed report to the AER outlining the specific causes and mitigating steps it has taken to address these breaches individually and more generally across its market systems.

1.4 Capacity data

STTM facility operators must provide daily information to the market regarding the quantity of natural gas it expects it will be able to deliver.[10] This includes the facility's expected capacity on days when deferrable maintenance may be scheduled for the facility.

In December 2013, we wrote to AGL over capacity data submissions to the Sydney hub from its upstream Camden facility in early November 2013. In this instance, AGL submitted information to the market that the Camden facility had an available capacity of 16TJ. However, for the same gas day, AGL only provided a 0TJ offer from the Camden facility. When queried about this difference, AGL explained that the 0TJ of offers reflected planned maintenance, however since this maintenance could be deferred on the day if required, the capacity submitted was 16 TJ. In AGL's view:

> "The capacity to deliver on future gas days, particularly where only one or two non-critical pieces of equipment was undergoing planned maintenance was still, in AGL's view, the rated capacity of the plant."

In response, we suggested this could be an area where it would be useful to provide guidance on how we intended to enforce compliance with this requirement.

On 10 June 2014, we presented a paper to the Gas Wholesale Consultative Forum (GWCF). The paper set out staff's interpretation of how to apply rule 414(1) to capacity data submissions when maintenance is deferrable. In particular, the paper suggested:

> "For deferrable maintenance situations, we consider this means that if at the time of submitting the capacity information to AEMO the STTM facility operator considers maintenance is more likely to go ahead than not, the capacity quantity should take into account the expected impact of the maintenance."

Following the GWCF we wrote to APA, Jemena, Epic Energy and SEAGas to ascertain how operators other than AGL account for capacity during maintenance situations. Respondents provided the following comments:

- if there was a risk to the three day forecast, deferrable maintenance activities would be deferred (SEAGas)
- planned maintenance is scheduled so as never to impact on the capacity to deliver to the hub (Epic)
- the capacity published reflects the configuration of a pipeline during a period in which maintenance is being undertaken and not whether the maintenance is deferrable or not (APA)

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[9] Data provided on disks will also be password protected, with password details distributed separately to data files.

[10] Clause 414(1) of the National Gas Rules.

- a capacity restriction would only be reflected in capacity data if maintenance was likely to go ahead i.e. a greater than 50 per cent chance (APA, Jemena)
- if work is being carried out at the delivery point and the work is deferrable and the recall time is relatively quick (e.g. 1 hour), capacity would not be reduced (Jemena).

View on best practice

In markets where decentralised decision making is premised on quality information, the submission of accurate and timely data, based on the best information available at the time is paramount. We consider if maintenance is planned but deferrable, it should be reflected in reduced capacity for the D-3 schedule if it is expected to go ahead i.e. greater than 50 per cent likelihood. Based on our inquiries we understand most planned maintenance will be scheduled 3 days out. If subsequent D-2 or D-1 scheduling information influences the operator to reconsider the planned maintenance, then the capacity should be updated if it no longer is expected to go ahead. For example:

- If there is an increase in prices after a submission of reduced capacity for D-3 in the Sydney Hub, AGL may as the operator of the Camden facility choose to defer the maintenance and reflect this as an update to D-2 or D-1 capacity data.
- If following a submission of reduced capacity, scheduled gas on the Eastern Gas Pipeline approaches that capacity, Jemena might choose to defer the maintenance and reflect this as an update to D-2 or D-1 data.

1.5 STTM demand forecasting update

Demand forecasts are the primary input for scheduling and forms the basis for calculating ex ante prices in the STTM. Poor demand forecasting leads to inefficiencies in dispatch whereby the ex ante price is set on the basis of a higher or lower quantity of gas than is required. It can also lead to higher MOS[11] payments in the STTM, whereby large amounts of gas are required to address the imbalance caused by inaccurate forecasts.

Rule 410(1) requires each STTM trading participant who expects to withdraw quantities of natural gas from a hub on a gas day to submit in good faith ex ante bids or price taker bids (and any revisions to those bids) to reflect the participant's best estimate of the quantity it expects to withdraw on that gas day (these bids in effect reflect each participant's demand forecast).

In 2012, the AER commenced a project in response to ongoing occurrences of inaccurate demand forecasts from a number of STTM participants. A particular concern was the uneven distribution, or bias of under and over forecasting of demand. We were also concerned by large avoidable demand forecast errors, for example, those caused by system errors.

Accordingly, throughout 2013, we applied metrics to each STTM hub to identify patterns in demand forecasting errors. Based on the results of our analysis, we contacted participants where large differences between forecast and actual demand or trends in either under and over forecasting were observed. Previous QCRs have presented information related to the demand forecasting performance of a number of participants (Incitec Pivot, Adelaide Brighton Cement Limited, Origin Energy and AGL Energy).

[11] MOS may also be influenced by other factors such as supply imbalances and physical constraints

Adelaide hub

In the Adelaide hub, average over and under forecast errors are relatively low at 4 per cent of total demand this year.[12] This represents a significant improvement on demand forecasting since 2012, whereby demand forecast errors were as high as 14 per cent of total demand (see figure 1.4).[13] In recent months, an increase in the size of under forecast demand errors has been observed. For example, under forecast errors were over 5 TJ for the majority of June or 7 per cent of demand.

Despite a recent increase in the magnitude of under forecast demand errors, over forecast demand errors continue to exceed demand forecast errors in the Adelaide hub. As set out below in figure 1.5, the rolling average of days under forecast for each month indicates there has been under forecast demand in the Adelaide hub for 45 per cent of days over the last 12 months. Meaning, for 55 per cent of the 12 month period, there was over forecast demand into the Adelaide hub. This represents a significant reduction from the end of 2012, whereby the rolling average of over forecast days was at 70 per cent of gas days.

Figure 1.4 Error as a proportion of total load and actual error volumes in the Adelaide hub[14]

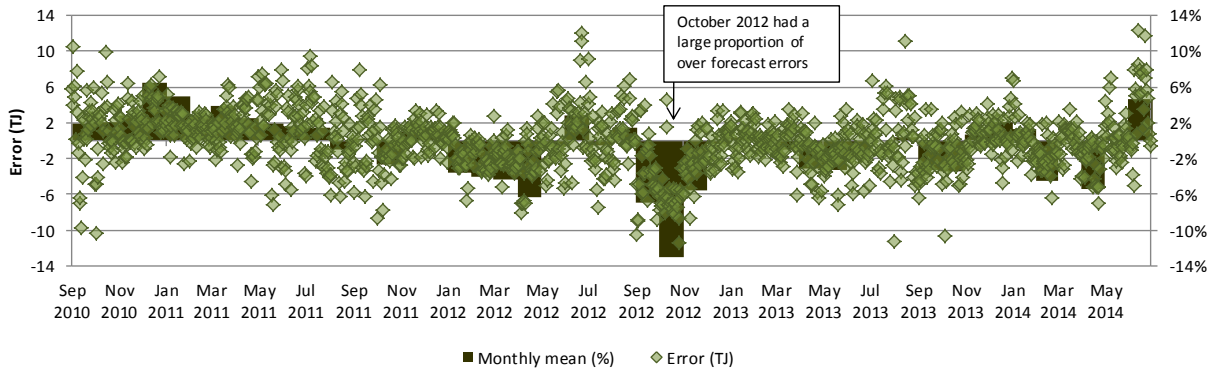
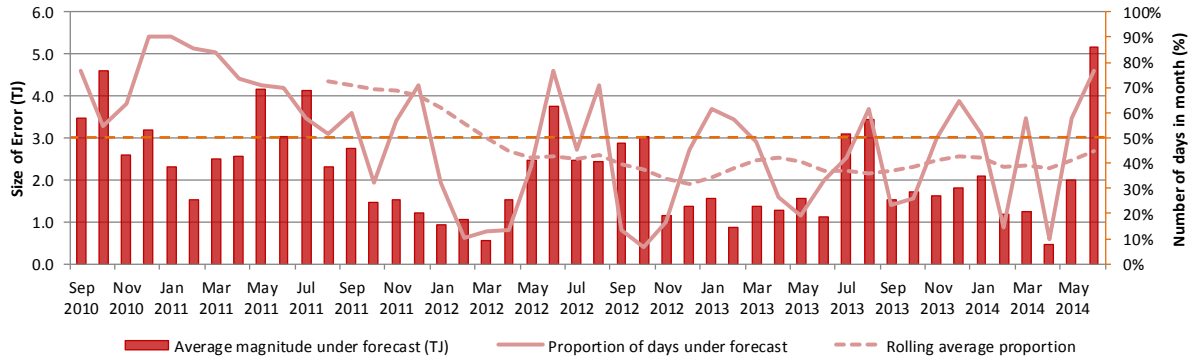


Figure 1.5 Days under forecast each month and actual error magnitudes in the Adelaide hub



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12 Analysis and figures showing demand in the Adelaide hub exclude Adelaide Brighton Cement, to remove the effect of unplanned outages (refer to the December 2012 QCR for more information).

13 October 2012 average over forecast error magnitude exceeded 14 per cent of demand, with aggregate demand over forecast on 29 days in that month.

14 Error = Actual – Forecast .

Sydney hub

Similar to the Adelaide hub, average forecast errors are relatively low at less than 4 per cent of total demand in the Sydney hub (see figure 1.6). However, a bias towards over forecast errors remains. In January 2014, the proportion of days over forecast (as a 12 month rolling average) increased to 70 per cent. However, this rolling average has since declined to approximately 60 per cent of days at the end of June (see figure 1.7). Conversely, a higher proportion of under forecast days occurred this quarter.

Figure 1.6 Error as a proportion of total load and actual error volumes in the Sydney hub

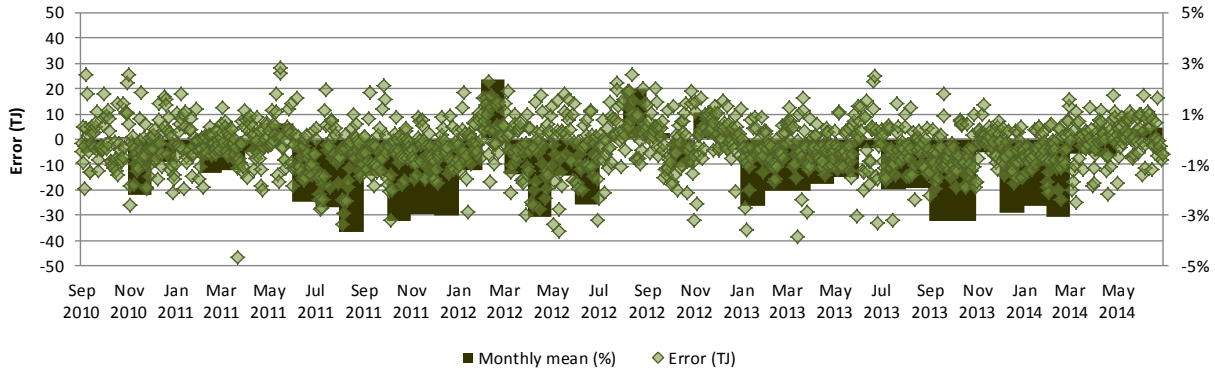
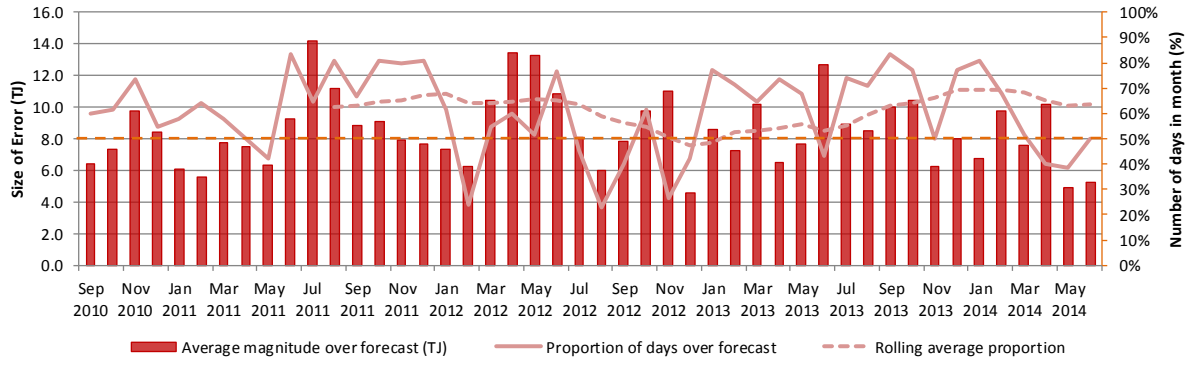


Figure 1.7 Days over forecast each month and actual error magnitudes in the Sydney hub



Brisbane hub

In Brisbane, average forecast errors remain low at around 3 per cent of total hub demand. In addition, we have seen an even distribution between the number of days which are over and under forecast days in the hub. However, despite this overall trend, we have observed a slight increase in the magnitude of under forecast errors in Brisbane. In particular, we have seen a higher number of larger forecast errors of more than 10 TJ this year. These deviations subsequently led to significant differences between the ex ante and ex post price on a number of occasions.

Figure 1.8 Error as a proportion of total load and actual error volumes in the Brisbane hub

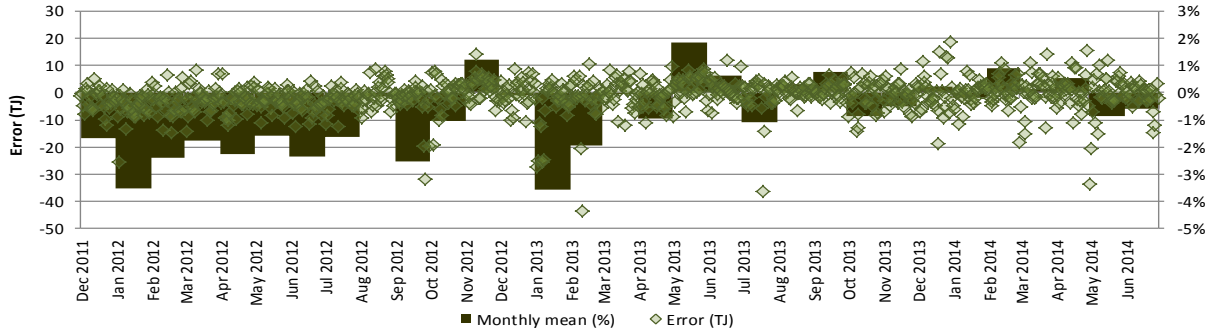
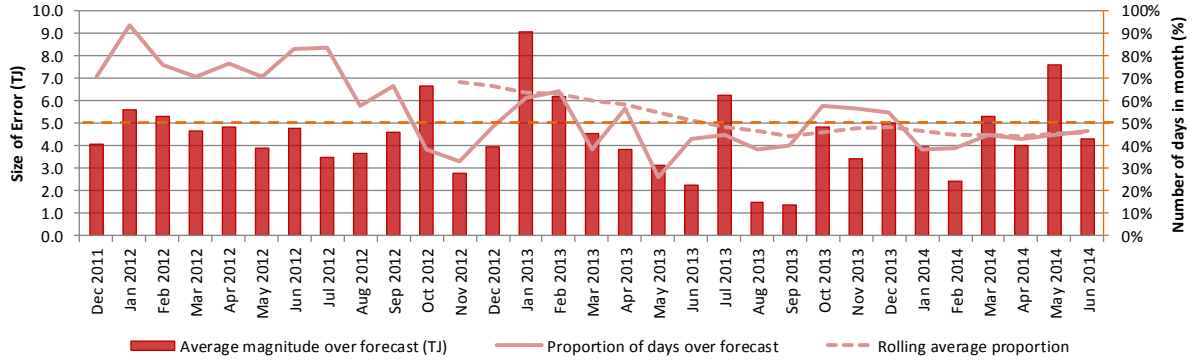


Figure 1.9 Days over forecast each month and actual error magnitudes in the Brisbane hub



Conclusions

Overall, current average demand forecast errors are relatively low compared to total demand in the STTM and in the case of Adelaide hub previous years' forecast errors. When errors do occur, they appear to be skewed to over forecasting. However, we note there has been a general trend in 2013/14 to a more even distribution of under and over forecasting in the Brisbane and Adelaide hubs. In the Sydney hub, there has been a recent reduction in a bias towards over forecasting, however the skew towards over forecasting remains more pronounced than other hubs and will continue to be an area of focus for the AER.

Beyond demand forecasting trends, the AER will continue to monitor individual forecast errors on a case-by-case basis. Where required, we will contact individual participants for further explanation to ensure those demand forecasts reflect best estimates. We will also report on the effects of inaccurate demand forecasting through our weekly monitoring reports and in QCRs from time to time.

Improvements in demand forecasting and impacts on MOS

As part of our demand forecasting project, we are also reporting on the impacts of demand forecasting upon the amount of MOS quantity required in the market.

Overall, there has been a reduction in MOS quantities over 2013/14, compared to the previous financial year.[15] However, while we consider that our focus on demand forecasting error is contributing to lower MOS outcomes, there are a number of other factors that may have contributed to the longer term MOS trends. This includes physical constraints in gas distribution networks, such as Envestra's gas distribution network in South Australia (see section 1.6 below). Furthermore, participants nominating or renominating different quantities to those scheduled on pipelines may also be impacting MOS levels across the STTM regions.

We will continue to monitor trends in MOS over 2014/15 and in particular, review MOS outcomes in the Adelaide hub following the opening of the Elizabeth zone valve in the South Australia. In addition, we will extend our analysis of demand forecasts to include those relating to the Victorian gas market in 2014/15.

1.6 Elizabeth zone valve

The Elizabeth zone valve in the South Australian gas distribution network was opened in June 2014. The opening of this valve will enable gas to be delivered from the SEA Gas pipeline into the Elizabeth part of Envestra's network. It is hoped this action will reduce the prevalence of counteracting MOS in the Adelaide hub and prevent the reoccurrence of high MOS payments which were experienced in the market last winter.

On the 25 June 2013 gas day in the Adelaide STTM hub 41 TJ of MOS was required. This resulted in a MOS service payment of $252 727–the highest MOS payment over the winter of 2013. At the time, we published a Significant Pricing Variation (**SPV**) report for this event in accordance rule 498(1)(b) and 498(2) of Part 20 of the Gas Rules, because the MOS service payment in the Adelaide hub exceeded the reporting threshold of $250 000.

Our investigation into the SPV found that the large requirement for MOS on the day was caused by the SEA Gas pipeline not being able to deliver its nominated quantity of gas into the Adelaide distribution network, and two physical issues had significantly impacted SEA Gas and MAP deliveries and increased MOS requirements. Firstly, the Elizabeth zone (part of the distribution network) was completely isolated from the SEA Gas pipeline, meaning that demand within the Elizabeth zone could only be serviced by the MAP. We found that this isolation may have been the single biggest contributor to counteracting MOS on that particular gas day, and a key contributor to counteracting MOS in the winter of 2013. Secondly, the pressure differences between the delivery points and within the distribution network limited the ability of the SEA Gas pipeline to supply parts of the distribution network (particularly towards the Taperoo part of the network). These two factors had increased the requirement for MOS as the ratio of gas flows scheduled on the SEA Gas relative to the MAP increases, especially on days of high hub demand. In our SPV report, we recommended that the issues be investigated by Envestra (the owner of the Adelaide distribution network at the time) as part of its network review.

For several years, including the 2013 winter period, the Adelaide network had been operated with a valve (valve 861) closed for operational requirements. When opened, valve 861 enables gas to be delivered from the SEA Gas pipeline into the Elizabeth part of the network. At the time, Envestra was reviewing its network, and specifically the physical design issues affecting the Adelaide hub. Envestra's review was to include modelling the consequences of opening the valve which was

[15] There has been a greater reduction when comparing the first half of 2014 to 2013.

preventing gas from the SEA Gas pipeline going into the Elizabeth zone, and also an engineering evaluation of whether the SEA Gas pipeline could provide the entire gas supply to the Adelaide hub.

Following our 2013 inquiries and discussions with participants about whether the valve could be reopened to address the issues we had identified, APA Group (responsible for Envestra's operations) concluded there would be no material adverse effects of re-opening the valve from an operational capacity and billing perspective. APA Group scheduled the valve to be re-opened on 3 July 2014. It will monitor the heating value impact around the network for the ensuing six months and will then assess whether there should be a uniform heating value for the Adelaide metropolitan area. We will continue to monitor the MOS outcomes following the opening of the valve.

Victorian gas market

Part 19 of the Gas Rules sets out participants' responsibilities in the Victorian gas market. The rules outline how wholesale gas is traded within the market and AEMO's obligations to operate the physical system. No significant compliance issues in the Victorian gas market were identified this quarter.

Bulletin Board

Part 18 of the Gas Rules sets out participants' responsibilities regarding the Bulletin Board. These obligations aim to facilitate greater transparency in gas production and gas pipeline flows to assist gas trading. The obligations also require participants to identify and report any potential conditions where curtailment of gas use might be necessary.

Under the Gas Rules, Bulletin Board facilities must submit a range of production and flow data to AEMO for publication on the Bulletin Board. This includes daily pipeline nominated and forecast delivery data[16] and daily production and pipeline flow data.[17] During the quarter, one facility operator failed on two occasions to submit firm nomination Bulletin Board data to AEMO on the relevant gas day. Further, four facility operators failed to submit daily flow Bulletin Board data to AEMO on 14 occasions.

We will continue to monitor participants' compliance with the Bulletin Board requirements of the Gas Rules. In particular, we will be engaging with Bulletin Board facility operators over the next quarter to ensure they are updating their short term capacity outlook in accordance with requirements of the Gas Rules.

[16] Rule 173 of the National Gas Rules.
[17] Rules 166 and 174 of the National Gas Rules.

2 Electricity

We are responsible for monitoring, investigating and enforcing compliance under the Electricity Law and Rules.

This part of the report provides an update on investigations, compliance matters and projects in the electricity market.

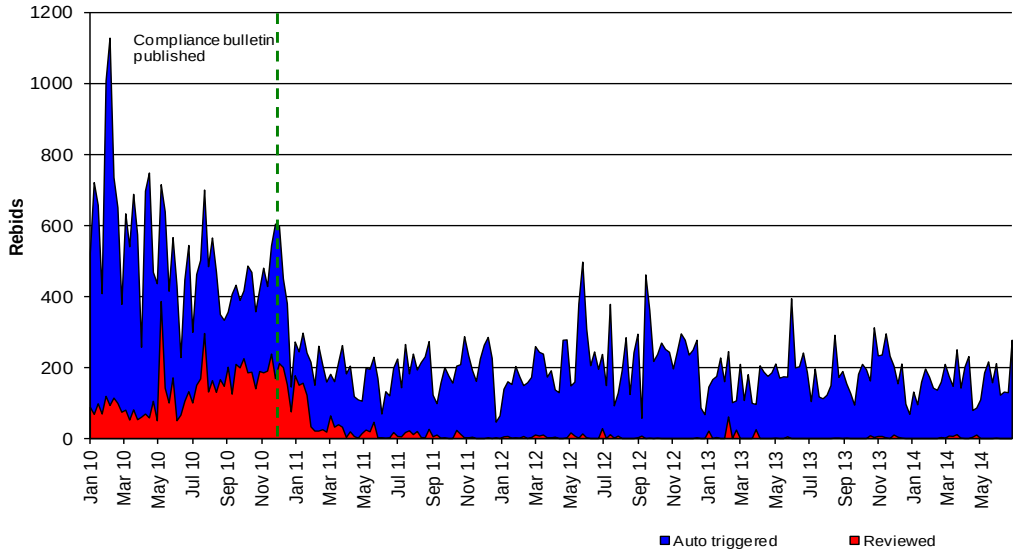
2.1 Rebidding

Scheduled generators and market participants operating in the National Electricity Market (**NEM**) submit electricity offers and bids for each half hour trading interval. The offers and bids include available capacity for up to 10 price bands, and can be varied through rebidding.[18]

We adopted a new strategy in relation to enforcing generator rebidding reason requirements in 2010.[19] Generators that submit offer, bid and/or rebid information that does not meet the requirements of the Electricity Rules will receive two warnings. On the third warning within six months, we will consider issuing an infringement notice. A participant's warning count is set to zero after six months.

Figure 2.1 shows that since 2010 the number of rebids detected by our internal compliance system has fallen markedly. The number of rebids which required further review continues to remain significantly low.

Figure 2.1 Rebids auto-triggered and reviewed per week



[18] Market participants must provide to AEMO, at the same time as a rebid is made, a brief, verifiable and specific reason for the rebid, plus the time at which the reason for the rebid occurred. Equivalent requirements apply where AEMO is advised, under clause 3.8.19 of the Electricity Rules, that a unit, service or load is inflexible. Clause 3.8.22A of the Electricity Rules requires that dispatch offers, dispatch bids and rebids are made in 'good faith'.

[19] In June 2012, we published an updated Compliance Bulletin No. 3 to make it clear that, for the purposes of administering the three stage process and issuing warnings, we will rely on the cumulative count of non-compliant bids for all generating units under the same portfolio. In other words, where a parent company employs a common trading team for the bidding of multiple generating units in its portfolio, irrespective of whether these generators are different registered participants, we will count any non-compliant bids by that trading team together.

There were two first warnings issued during the June quarter. Both warnings were due to the participants not submitting a time adduced in their rebid reasons. Participants notified us of errors in their rebids on 17 occasions during the quarter and three participants had their warning counts reset to zero.

2.2 Snowy Hydro: alleged failure to comply with AEMO dispatch instructions

The AER has instituted proceedings in the Federal Court of Australia against Snowy Hydro[20] for alleged contraventions of the Electricity Rules.

The AER alleges that Snowy Hydro failed to follow dispatch instructions issued by AEMO on nine occasions in 2012 and 2013, in breach of the Electricity Rules which require generators to comply with AEMO dispatch instructions. The AER alleges that, on each occasion, Snowy Hydro generated substantially more power than the dispatch instruction required it to generate, and earned a greater trading amount from each transaction than it would have earned if it had complied with the dispatch instruction.

Compliance with dispatch instructions is mandatory to ensure the power system remains secure. AEMO relies upon conformance with dispatch instructions to ensure it can effectively perform its functions as both power system operator and market operator for the NEM.

The AER is seeking declarations, injunctions, penalties and costs.

2.3 Lumo Energy - Market management system access

Lumo Energy paid an infringement penalty of $20,000 for enabling unauthorised persons to have access to AEMO's market systems. The AER issued the infringement notice to Lumo Energy after undertaking a 5 month investigation into Lumo Energy's conduct.

The AER launched an investigation into Lumo Energy, after it was alleged that Lumo Energy had made changes to its IT network that facilitated access to AEMO's market systems which was not consistent with clause 3.19(c) of the Electricity Rules. Clause 3.19(c) of the Electricity Rules requires registered participants to comply with the Market Management Systems Access Procedures. The Market Management Systems Access Procedures prescribe obligations which prohibit, among other things, unauthorised persons from accessing AEMO's market systems.

AEMO's market systems include the Market Settlement and Transfer Solution (MSATS) system. The MSATS system facilitates customer transfers and market settlement in the NEM. The MSATS system, which is administered by AEMO, holds an array of data relating to each connection point. The MSATS system also facilitates settlement processes in the NEM. Participant access to the MSATS system is defined by the access procedures.

On 16 December 2013, AEMO advised the AER that Lumo Energy had made changes to its IT network that facilitated access to the MSATS system which was not consistent with the access procedures. In response, the AER sought a range of information from Lumo Energy to ascertain the validity of this information.

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[20] Snowy Hydro is an electricity generator owned by the New South Wales, Victorian and Commonwealth Governments.

The AER formed the view that Lumo Energy breached rule 3.19(c). The AER consider that Lumo Energy had enabled:

- unauthorised IP addresses to be exposed to the MSATS system and
- the transmission of unencrypted MSATS data over the public internet.

The AER issued Lumo Energy with an infringement notice on 19 May 2014, alleging it had breached rule 3.19(c). Lumo paid the infringement penalty on 21 May 2014. Payment of the $20,000 infringement penalty does not represent an admission by Lumo Energy that it has breached the Electricity Rules.

2.4 Targeted compliance review – Market management system access

Targeted compliance reviews form an important part of our monitoring program. The reviews explore participants' compliance practices and aim to improve stakeholder understanding of obligations. The AER will generally choose the obligation on the basis of its risk assessment of the Electricity Rules, whereby obligations are identified as having a medium to high risk and impact will be selected for review. We also take into account previous industry performance with respect to the obligation.

In this quarter, we decided to target clause 3.19(c) of the Electricity Rules. As identified above in section 2.3, this rule requires registered participants to comply with AEMO's Market Management Systems Access Procedures. We selected this obligation for two reasons, namely its high impact ranking in our risk assessment and the matter involving Lumo Energy. Through this review process, we wanted to ensure other registered participants had sufficient processes in place to achieve compliance with AEMO's Market Management Systems Access Procedures and therefore, rule 3.19(c). In particular, we wanted comfort that if registered participants engaged third parties to provide services, these third parties would also act according to the requirements of the Market Management Systems Access Procedures. [21]

We wrote to Origin Energy, Simply Energy and Red Energy to ascertain their compliance approach with respect to rule 3.19(c). In particular, we asked the three retailers to provide details of their systems and procedures to comply with this rule requirement, including any arrangements it has in place to ensure contracted third parties achieve ongoing compliance.

Overall, the retailers' responses appear to provide limited but sufficient detail regarding their approach to compliance with the Market Management Systems Access Procedures and therefore, rule 3.19(c). Each party emphasised their commitment to ensuring access to AEMO's market systems is isolated from internet. Further, where third parties are being used, the retailers set out the mechanisms they use to ensure the third party complies with relevant system security requirements. We will continue to review these requirements over the coming quarters, including seek supplementary information regarding system security training for third party providers and details regarding participant's permanent connection AEMO's market systems.

[21] The Market Management System Access Procedures, which are prescribed by AEMO, set out a range of rule and non-rule enforceable requirements pertaining to market system access. Rule enforceable obligations include ensuring traffic from the Internet and the registered participant's internal networks are isolated from their connection to AEMO's Electricity Market Management Systems.

2.5 Meter churn procedures – request for no action

The Australian Energy Market Operator's Meter Churn Procedures establish processes to manage the physical exchange of meters alongside customer transfers, meter data changes, including updates to NMI standing data. However, some elements of the Meter Churn Procedures are inconsistent with the Electricity Rules. [22] As a result, registered participants who have developed processes to comply with the Meter Churn Procedures are non-compliant with certain metering obligations in chapter 7 of the Electricity Rules.

In March 2014, AEMO sought comfort from the AER that it would not pursue enforcement action against these registered participants until it had an opportunity to revise the Meter Churn Procedures. AEMO suggested to the AER that its revision process would be completed by December 2014.

On the basis of the information provided, it is unlikely we would pursue enforcement action against registered participants who developed processes to comply with the Meter Churn Procedures but are subsequently non-compliant with the Electricity Rules. However, we expect the Meter Churn Procedures and registered participants' meter churn processes to be compliant with the Electricity Rules by January 2015.

2.6 Technical audits

Auditing is one mechanism we use to verify and assess compliance by registered participants with their obligations. The audits aim to ensure participants have robust and effective compliance programs in place that are consistent with Good Energy Industry Practice.

We conduct regular technical compliance audits in the electricity sector of generators and network service providers. These audits generally focus on the Electricity Rules clauses 4.15 and 5.7.4, particularly the requirement on electricity generators and network service providers to institute and maintain a compliance program in accordance with prescribed requirements.

In particular, the mandated compliance program must:

- include procedures to monitor the performance of the plant in a manner that is consistent with good electricity industry practice
- provide reasonable assurance of ongoing compliance with applicable performance standards registered with AEMO.

2.6.1 ElectraNet

This quarter, the AER carried out a technical compliance audit of ElectraNet, South Australia's transmission network provider and the third such participant targeted by the AER. The key findings of this audit included:

- ElectraNet having a corporate governance structure and an overarching risk-based compliance framework across its legal and operational areas that is similar to those of equivalent network businesses;

[22] For example, unlike the Electricity Rules, the Meter Churn Procedures enable someone other than the Responsible Person to appoint the metering provider for a connection point.

- scope for improving the technical compliance program in place by developing a more holistic understanding of the detailed performance of protection and control systems, which under ElectraNet's current model are maintained through service agreements;
- ensuring that technical knowledge leakage does not significantly impact on the performance of protection and control systems over time, particularly given the procurement model employed; and
- also ensuring that the management of service and coordination arrangements are robust and effectively administered, in the interests of ensuring ongoing compliance in this area.

ElectraNet has already recognised the need for improvements in the above areas by engaging in a series of initiatives to bolster the effectiveness of its technical compliance program. A key aim of this is ensuring that as expertise leaves the industry, its internal knowledge systems and expertise are sufficient to fill any void. To this end, following a relatively recent business restructure, ElectraNet has moved to create an Asset Management Division and Network and Asset Management Performance Groups, while upgraded data systems, field and analytics tools are scheduled to be implemented over the upcoming months.

AER staff are therefore of the view that, once the above initiatives are fully implemented, the technical compliance program of ElectraNet should be more effective and result in the technical matters covered by this audit being addressed in a manner that is more aligned to good electricity industry practice. To this end, ElectraNet has committed to keeping the AER informed of progress with these initiatives.

2.7 Jurisdictional derogations

Chapter 9 derogations exempt Victorian smelter traders, New South Wales power traders and Queensland nominated generators (for the purposes of exempted generator agreements) from complying with the Electricity Rules to the extent there exists:

- any inconsistency between the Rules and a contractual requirement under the relevant agreement between the government and other entities
- any other specified exemption in the jurisdictional derogations.[23]

The relevant participants must give us notice of any act or omission which partly or wholly constitutes non-compliance with the Electricity Rules. No instances of non-compliance were reported this quarter.

2.8 Current transformer testing

The Electricity Rules require current transformers to be tested every 10 years, unless it is the subject of an asset management strategy which has been approved by AEMO.

In 2011, AEMO alerted the AER to a widespread failure by Responsible Persons **(RPs)** to test low voltage CTs in accordance with the Electricity Rules. In response we released a Compliance Bulletin outlining our expectations and seeking for RPs to demonstrate a willingness to comply with the testing requirements by testing a sample of their metering installations from 1 July 2012. Following a review

[23] Refer to National Electricity Rules clauses 9.4.3 (smelter trader: Vicpower Trading), 9.12.3 (power traders: Delta Electricity and Macquarie Generation) and 9.34.6 (nominated generators: CS Energy and Stanwell Corporation).

of testing undertaken to 30 June 2013, we established that Red Energy did not complete the required testing. In response, the AER issued an infringement penalty notice to Red Energy in February 2014.[24]

In 2014, we will continue to work with AEMO to ensure RPs comply with the CT testing requirements of the Electricity Rules. In July 2014, AEMO will provide the AER with advice regarding industry CT testing levels. Based on this information, the AER may seek further information from RPs and possibly, undertake further enforcement action.

[24] Red Energy paid the infringement notice penalty on 21 March 2014.

Appendix A Shortened forms

Shortened form	Full title
ACCC	Australian Competition & Consumer Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
AMI	Advanced Metering Infrastructure
CATS	Consumer Administration and Transfer Solution
Electricity Law	National Electricity Law (Schedule to the National Electricity Act)
Electricity Rules	The National Electricity Rules made under Part 7 of the Electricity Law
FCAS	Frequency Control Ancillary Service
Gas Law	National Gas Law (Schedule to the National Gas Act)
Gas Regulations	The *National Gas (South Australia) Regulations* made under the National Gas Act
Gas Rules	The National Gas Rules made under Part 9 of the Gas Law
GEIP	Good Energy Industry Practice
GJ	Gigajoule
LCA	Linepack capacity adequacy
MAP	Moomba to Adelaide pipeline
MOS	Market Operator Service
MSATS	Market Settlement and Transfer Solution
MT PASA	Medium Term Projected Assessment of System Adequacy
MW	Megawatt
MWh	Megawatt hour
National Electricity Act	*National Electricity (South Australia) Act 1996* (South Australia)
National Gas Act	*National Gas (South Australia) Act 2008* (South Australia)
NEM	National Electricity Market
NMI	National Meter Identifier
QCR	The AER's quarterly compliance report
RIT-T	Regulatory investment test for transmission
RP	Responsible Person
SCADA	Supervisory control and data acquisition
STTM	Short Term Trading Market
SWN	System Wide Notice
TJ	Terajoule