

28 March 2008

Dr John Tamblyn
Chair
Australian Energy Market Commission
PO Box H166
AUSTRALIA SQUARE NSW 1215

Dear Dr Tamblyn

AEMC Review of Demand-side Participation

The Energy Networks Association (ENA) welcomes this opportunity to respond to the Australian Energy Market Commission's (AEMC) call for comments on the draft recommendations in the NERA Economic Consulting report "Review of the role of demand-side participation in the National Electricity Market (NEM)", which was drafted as part of Stage 1 of the AEMC Review.

ENA is the peak national body representing gas and electricity distribution businesses throughout Australia.

Energy network businesses deliver electricity and gas to over 12 million customer connections across Australia through approximately 800 000 kilometres of electricity lines and 75 000 kilometres of gas distribution pipelines. These distribution networks are valued at more than \$35 billion, and each year energy network businesses undertake capital investment of more than \$5 billion in network reinforcement, expansions and extensions.

ENA supports this AEMC review as an opportunity to identify and address ways that regulatory frameworks can ensure commercial, efficient and feasible demand side participation occurs in the Australian energy market. This position is reflected in ENA's contributions to the Australian Government's work on demand management related issues over the last two years. In particular we have provided comprehensive submissions to the Ministerial Council on Energy (MCE) papers dealing with "Network Planning and Connections Arrangement" in May and October 2007. We also lodged a submission on 1 February 2008 with the AEMC in response to the Commission's consultation on the Total Environment Centre's (TEC) proposed rule change related to the application of demand management to transmission networks and the wholesale market. In this context, ENA welcomes the incorporation of AEMC consideration of the TEC proposal as part of its wider review rather than in isolation, a concern raised in our submission.

More recently ENA released its enclosed *Demand Management – Regulatory and Policy Framework* which it should be noted, recommends the current AEMC review of regulatory arrangements supporting network demand management (Rec 10. p18).

The Framework brings together in one document the ENA's extensive knowledge and experience in dealing with demand management issues and provides a comprehensive description of what demand management is, how it is regulated and what needs to be done to ensure that policy and regulatory frameworks are not barriers to investment in non-network options. More specifically, in terms of the NERA papers draft recommendations, ENA's Demand Management Framework covers many of the issues NERA raises and provides the rationale for ENA's positions on matters relating to the electricity pricing, regulatory investment test, network planning, and the provision of information.

Electricity Pricing

ENA concurs with the NERA paper on the vital role of cost reflective pricing in realising optimal DSP and the possible benefits of smart meter roll out to facilitate demand responses. While the need for an examination of regulatory constraints to efficient pricing as a first step is acknowledged ENA is concerned that retailers do not have sufficient incentive to pass-on differential network tariffs to end users. In this context, ENA's Framework document recommends that barriers or disincentives for retailers to pass through time of use and other cost-reflective price signals should be removed (Rec 22, p29).

Regulatory Investment Test (RIT)

ENA believes that any reforms to the regulatory framework should allow network businesses to adopt efficient network and non-network options on an equal basis. (Rec 2, p11). Consequently, ENA concurs with the views in the paper which state that; "it is important that decision making criteria (in the regulations) do not induce a bias against demand side alternatives".

However, ENA is very concerned that the NERA papers recommendations will lead to a reversal of the current perceived bias such that the outcome will be biased towards demand side options. In addition, the incorporation on national market benefits as sought by the MCE provides for the possibility that network providers will be required to opt for a non-network solution even where a business case has not been established.

ENA's concern is reflected in the draft recommendations on p39 of the paper where it advocates that the RIT define "wider national benefits" for non-network options. ENA notes the approach adopted to addressing network demand management issues must seek to balance the goal of demand management policy issues against other network obligations. In this regard ENA expects Stage 2 of the Review to cover this issue including the matter of ensuring that the regulatory framework needs to recognise the need to balance risks and rewards to ensure that network providers only engage in commercially viable non-network options.

ENA also takes issue with the Draft recommendation that risk adjusted benefits and costs be applied to account for the different risks between alternative options. While this has appeal in theory as a means of addressing reliability risk related to non-network options, in practise, ENA recognises there is no objective measure of the risk. Therefore arbitrary risk adjusted outcomes are expected. The result could put in jeopardy the ability of network providers to meet their reliability obligations. In its Framework paper ENA proposes that the AEMC consider appropriate mechanisms to manage reliability risk so that distribution businesses are not disproportionately penalised (Rec 17, p25) and that the AEMC and the Australian Energy Regulator (AER) consider appropriate mechanisms and incentives to support network demand management pilots and trials (rec18, p26) as a way of managing demand response uncertainty.

Provision of Information and Network Planning

The NERA paper (p32) suggests that improving the information provided by network service providers for alternative options to network investment should make them more attractive and recommends rules that adequate information be provided.

In its October 2007 Submission to the MCE responding to the NERA/Allen paper on "Network Planning and Connection Arrangements" ENA stated that the evidence on this issue indicated that the mere provision of detailed information did not deliver the uptake of non-network options. (p12 of the Submission). The conclusion was that economic incentives that change the underlying risk profile for non-network options are an essential to affect a change.

Notwithstanding the above, ENA supports the integration of network demand management and the provision of information to the community as this improves the transparency of network business activity, albeit, without changing the underlying business case for increasing demand management alternatives. Accordingly, the ENA Framework recommends AMC consider developing nationally consistent information and planning regime (Rec 20, p27).

Should you have any queries in relation to the above please do not hesitate to contact me.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'ABlyth'.

Andrew Blyth
Chief Executive