



## EBSS and Demand Management Expenditure

Final rule determination issued 22 December 2011

**This rule requires the AER, in designing and implementing the Efficiency Benefit Sharing Scheme (EBSS), to consider the possible effects of the scheme on a transmission operator's incentive for the implementation of non-network alternatives. The rule strengthens the scope and certainty for transmission operators to pursue demand management options and find an efficient balance between the need for additional network investment and the value of demand**

### Background

The transmission network is the set of high voltage wires and associated assets that transports electricity long distances. In the National Electricity Market (NEM), this network is owned and operated by a number of transmission network service providers (TNSP). TNSPs must ensure that the transmission network supplies all the distribution networks with enough electricity to meet consumers' needs.

The National Electricity Rules (NER) require the AER to establish and apply an EBSS for TNSPs.

An EBSS should encourage cost efficiency by providing an incentive mechanism through which TNSPs can earn additional revenue or be penalised. This depends on whether the business beats or exceeds targets for its operating expenditure in each year of the regulatory control period.

### Problem identified

The MCE submitted a rule change request in November 2010 noting that demand-side participation (DSP) solutions are largely in the form of on-going operating expenditure, the Commission's DSP review found that the EBSS may potentially create disincentives for a TNSP to consider efficient non-network alternatives.

This is because expenditure on demand-side related solutions are largely in the form of on-going operating expenditure. The EBSS can therefore potentially create a disincentive for a TNSP to consider efficient non-network alternatives, as it may lead to reduced financial rewards or even penalties if the expenditure results in actual operating expenditure being more than the forecast.

Currently, the EBSS framework does not require the AER to consider how the scheme might impact on a TNSP's incentives to pursue efficient DSP solutions.

### Rule change request

In order to address the disincentive to undertake efficient DSP solutions the MCE proposed a rule to expand the scope of the EBSS rule to require the AER to consider the scheme's effect on a TNSP's incentive to incur non-network alternative expenditure.

The rule change process commenced in June 2011 and on 19 September the Commission published a draft rule determination and a draft rule. The Commission proposed to make the rule proposed by the MCE.

**This rule provides TNSPs with more confidence to pursue demand management options**

### Final rule determination

The AEMC's final rule determination notes that the AER has already moved to recognise the impact of the EBSS on a TNSPs' incentives for pursuing DSP solutions by excluding non-network alternative expenditure from the EBSS. While the AER's more recent decisions on the EBSS effectively neutralises the materiality of the problem identified in the rule change request, the current EBSS framework for TNSPs does not ensure that the AER will consistently consider the incentives for non-network alternative expenditures when it applies the EBSS to TNSPs revenue determinations.

The current lack of certainty and consistency in how a TNSP's non-network alternative expenditure may impact on its EBSS reward/penalties for the next regulatory period makes it unlikely that a TNSP will take a risk by substituting more economically efficient demand- side solutions with network solutions.

The final rule clarifies the issue by making it an explicit requirement for the AER, in designing and implementing the EBSS, to consider the scheme's efficiency reward/penalty effects on incentives for a TNSP to undertake non-network alternative expenditure on a consistent basis. This should provide TNSPs more confidence to pursue demand management options and find an efficient balance between the need for additional network investment and the value of flexible demand.

The final rule does not define or categorise non-network alternative expenditures for the purposes of the EBSS. The Commission believes that objective of the final rule is more likely to be achieved by allowing the AER discretion in deciding the types of non-network alternative expenditure it will exclude from the EBSS on a case by case basis. In this regard, the final rule provision is consistent with the treatment of non-network alternative expenditure in the EBSS framework for Distribution Network Service Providers.

### Further information

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