



Mr Eamonn Corrigan
Director
Australian Energy Market Commission
PO Box A2449
Sydney South, NSW 1235

11 October 2012

Dear Mr Corrigan

Re: EPR002 - Power of choice review – giving consumers options in the way they use electricity – Draft Report

1. Introduction

CitiPower and Powercor Australia (**the Businesses**) welcome the opportunity to comment on the Australian Energy Market Commission's (**Commission**) "Power of choice – giving consumers options in the way they use electricity – Draft Report" (**Draft Report**) and "Power of Choice Review Draft Report Supplementary Paper" (**Supplementary Paper**), issued on 6 September 2012.

2. Background and context

The Draft Report and Supplementary Paper mark the second step in the Stage 3 Demand Side Participation Review (**Stage 3 DSP Review**), the purpose of which is to "identify market and regulatory arrangements that enable the participation of supply and demand side options in achieving economically efficient demand/supply balance in the electricity market"¹.

The Businesses welcome this review and note that in developing the recommendations set out in the Draft Report, the AEMC has acknowledged concerns raised by the Businesses, and other distribution network service providers (**DNSP**), in their submissions on Directions Paper², particularly in relation to the economic regulatory framework set out in Chapter 6 of the National Electricity Rules (**Rules**).

¹ MCE terms of reference to the AEMC. Found at:
<http://www.aemc.gov.au/media/docs/MCE%20Terms%20of%20Reference-35e6904a-e39d-4348-8ad5-1a7970af354d-0.pdf>

² "Power of choice review – giving consumers options in the way they use electricity – Directions Paper" (**Directions Paper**) issued on 23 March 2012

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3. Issues

Attachment 1 of this submission details the Businesses' preferred positions on each of the issues raised in the Draft Report. A summary of the Businesses' key positions is set out below:

Flexible (cost reflective) pricing

The Businesses:

- support cost reflective tariffs and locational pricing signals, as enabled by the installation of smart meters, as they may assist in promoting the efficient use of the network;
- support the proposed "time varying network tariff" approach set out in the Draft Report, subject to:
 - the removal the consumption thresholds, which are complex and unnecessary. The Businesses propose that a simpler more transparent approach would be to deem all small customers to be on "time varying network tariffs". Importantly, this would not prevent customers from electing a flat rate tariff from their retailer. Retailers operate in a competitive environment and will offer a variety of tariff options, including flat tariffs, to meet consumers' demands;
 - flexibility to introduce other types of cost reflective tariffs that may assist in promoting the efficient use of the network including capacity / volume based tariffs and dynamic or critical peak pricing tariffs; and
 - clarification of how the proposed "time varying network tariff" approach will accommodate the recently announced Victorian Government's "flexible tariff" initiative, which will commence from mid-2013.
- consider that the pricing principles under the Rules already accommodate cost reflective tariffs and that increasing prescription in the pricing principles will only act to reduce flexibility for DNSPs to develop innovative and efficient network tariffs relevant to their own circumstances (that reflect the nature of their customer base) and preferences.

Provision of smart metering infrastructure and functionality

The Businesses:

- support a mandated and accelerated approach to the roll-out of AMI (smart meters). The Victorian mandated AMI roll-out will take around five years to complete and even longer to realise the full suite of benefits and opportunities created by AMI. A non-mandated approach would take far longer to deliver – this would depend on the level of acceptance of smart meters from customers. Under a non-mandated approach, it is questionable whether the benefits and opportunities created by smart meters would ever be realised;
- support DNSPs leading any mandated roll out on the basis of the cost-benefit analysis undertaken for the Standing Council on energy and Resources (SCER) in 2008 (then the Ministerial Council on Energy (MCE)) and the success of the AMI roll-out in Victoria. Any change to the SCER's Statement of Policy

Principles and the National Electricity Law (**NEL**), which require DNSPs to undertake any jurisdictional mandated roll out, should be supported by a full Regulatory Impact Assessment to ensure consistency with the national electricity objective (**NEO**). Benefits associated with a DNSP-led mandated roll out, as identified in the cost-benefit analysis, include amongst other things, effective communications technology and scale economies. A piecemeal roll out of smart meters, without practical interoperability and clear procedures, may result in:

- cost inefficiencies due to system incompatibilities;
- inefficient and costly duplications in communications systems; and
- multiple Meter Data Management systems (back office IT).

Further, a piecemeal rollout may inhibit realisation of customer benefits leveraging off advanced metering, which were identified in a report prepared for the Businesses by PricewaterhouseCoopers (**PWC**)³ in 2009. The PWC Report identified the positive customer benefits that can be realised by leveraging investment in AMI, in the areas of network management and operation from the Victorian distributor led mandated roll out. A copy of this report can be provided on request;

- support the SMI Minimum Functionality Specification (**SMI Specification**) as a basis for any future national specification, subject to the introduction of grandfathering arrangements to ensure compliance of the AMI meters in Victoria (which comply with a different specification set out in the relevant Victorian Order in Council (**OIC**)⁴). The SMI Specification has been heavily consulted on over a long period and therefore it is unclear why it would not be adopted;
- emphasise that exit fees are essential to ensure that DNSPs are fully recompensed for the fixed and variable costs they have and would incur for any metering installation that is no longer required. In Victoria, for AMI meters, this includes the meter, the communications infrastructure and IT support systems. This should be recovered from the relevant customer, on the basis that the costs are directly attributable to that customer; and
- encourage the AEMC to consider, and fully consult on, other possible arrangements, to avoid meter churn associated with retailer churn (where the retailer is the Meter Provider), than those considered in the Draft Report. Other possible options include meter leasing arrangements or franchise metering areas.

Distributed generation

The Businesses support:

- the potential changes to regulatory incentives under Chapter 6 of the Rules, including allowing:
 - expenditure associated with projects approved under the Demand Management and Embedded Generation Connection Incentive Scheme

³ CitiPower and Powercor AMI Leveraged Projects: An assessment of the justifiable need for investment in additional AMI capabilities, PWC October 2009

⁴ AMI Specifications OIC, 12 November 2007

(DMEGCIS)⁵ to be treated in the same manner as all other operating and capital expenditure (**capex**);

- DNSPs to retain the value of capex savings resulting from the implementation of a demand side participation (**DSP**) project;
 - DNSPs to earn a share of market benefits arising from investment in DSP that accrue to the other sectors of the supply chain; and
 - DNSPs to recover foregone revenue from the implementation of DSP, including DSP tariff based projects.
- the proposal to potentially incorporate high level principles into the Rules to guide the AER's development of an innovation incentive scheme; and
 - the draft recommendation that the AER should consider allowing DNSPs to own and operate distributed generation assets when developing the national ring fencing guidelines.

Customer engagement to provide DSP products

The Businesses support:

- allowing commercial relationships to develop between parties along the supply chain, either directly or through intermediaries; and
- third party participation in the National Electricity Market (**NEM**), however the Businesses note that they should be subject to the relevant requirements under the National Energy Customer Framework (**NEFC**) or the Rules to ensure safety, system security and a level playing field.

4. Closing

The Businesses would welcome the opportunity to discuss further the issues raised in this submission with the AEMC.

Should you have any further questions in relation to this submission, please do not hesitate to contact Stephanie McDougall, Manager Regulatory Projects, on (03) 9683 4518 or at smcdougall@powercor.com.au.

Yours sincerely



Brent Cleeve

MANAGER REGULATION

⁵ In Victoria this is referred to as the Demand Management Incentive Scheme (**DMIS**)

ATTACHMENT 1: THE BUSINESSES' RESPONSES TO THE QUESTIONS RAISED IN THE DIRECTIONS PAPER

Questions posed in Draft Report		The Businesses' response
Chapter 2 - Facilitating consumer access to electricity consumption information		
1.	<i>What should be the minimum standard form and structure of energy and metering data supplied to consumers (or their agents)? Should these arrangements differentiate between consumer sectors (i.e. industrial / commercial and residential)</i>	The Australian Energy Market Operators (AEMO) Meter Data File Format (MDFF) specification could be adopted. This conveys sufficient information and does not require significant development or investment.
2.	<i>When do you think it is appropriate for a retailer (or responsible party) to charge a fee for supplying energy and metering data to consumers or their agents?</i>	This is a matter for these parties to decide, however, to the extent that the retailer or responsible party incurs a cost for providing this data, then it would be expected that they would provide the data on a fee for service basis.
3.	<i>Do you agree that general market information should be published on consumer segment load profiles to inform the development of DSP products and services to consumers?</i>	It is important that consumers are aware of the impact of their consumption and demand decisions as this will assist them to better manage their energy consumption patterns and reduce their electricity bills. The installation of AMI in Victoria will enable consumers to access information on their own load profiles, however it will not provide load profile information on consumer segments. The Businesses consider that such information would be useful to consumers as it will inform them about how their energy consumption compares to the average energy consumption of particular consumer segments.
4.	<i>Is AEMO the appropriate body to publish such information, or should each DNSP be required to provide such information particularly where data will be at the feeder level where accumulation meters are installed?</i>	This could be provided by retailers who should have access to the demographic information required to develop consumer segments.
Chapter 3: Engaging with consumers to provide DSP products and services		
Energy services to residential and small business consumers		
5.	<i>What specific criteria could be used to determine whether elements of the NECF (i.e. marketing code) apply to third parties providing DSP energy services to consumers? That is, beyond Australian Consumer Law?</i>	The Businesses consider that third party participation in the NEM should be governed under the Rules and or the NEFC. In particular, there should be clear requirements relating to the following matters for third party providers: <ul style="list-style-type: none"> • how third parties interact with DNSPs and retailers; • required qualifications and training of third party providers; • consumer protection measures;

		<ul style="list-style-type: none"> • privacy requirements; • dispute management processes; and • enforcement for non compliances. <p>The Businesses support further additional requirements for demand aggregators including arrangements which govern how load is removed and reinstated so as to ensure that the electricity supply and operation of the market is not compromised.</p>
6.	<i>What requirements should be in place for these third parties? For example, what should be the form of authorisations/accreditations?</i>	<p>Refer to the Businesses' response to question 5.</p> <p>To the extent that the services provided by third parties are the same as those provided by retailers and DNSPs, then third parties should be subject to the same provisions as retailers and DNSPs to ensure a level playing field.</p>
7.	<i>Do you agree that existing rules and guidelines should be amended to clearly outline the circumstances when distribution businesses are able to directly contract with residential and small consumers to deliver DSP network management services/programs?</i>	<p>The Businesses support an approach that allows commercial relationships to develop between parties along the supply chain, either directly or through intermediaries.</p>
Chapter 4: Functional Specification of meters in the Rules		
<i>Functional Specification of meters in the Rules</i>		
8.	<i>Should the minimum functionality specification for meters be limited to only those functions required to record interval consumption and have remote communication? Alternatively, should the minimum functionality include some, or all, of the additional functions specified in the SMI Minimum Functionality Specification?</i>	<p>The Businesses support the SMI Specification as a basis for any future national functionality specification. The SMI Specification contains both metrology functions, which relating to measuring consumption, as well as non-metrology related functions, which capture DNSPs operational savings possible with a smart meter and facilitate the increased ability for the consumer to manage its consumption. This has been widely consulted on over a long period and therefore it is unclear why this would not now be adopted.</p> <p>The Businesses note however that there are some differences between the SMI Specification and the functionality specified for Victoria in the AMI Specifications Order in Council. Therefore, should the SMI Specification be adopted, grandfathering compliance arrangements for the Victorian AMI meters should be developed.</p> <p>Alternatively, the Businesses support the functionality set out in the Victorian AMI Specifications OIC. This provides for remote meter reading, remote connection and disconnection, as well as further advanced functionality covering quality of supply monitoring, outage detection, tamper detection, controlled load management and supply capacity control.</p> <p>The Businesses consider that the scope of functionality in the SMI Specification, or alternatively the</p>

		Victorian AMI Specifications OIC, is necessary to ensure that the benefits to consumer and the wider market arising from the introduction of AMI meters can be achieved in an efficient, orderly and timely manner.
Arrangements to support commercial investment in metering technology		
9.	<p><i>Does the separation of the provision of metering services from retail energy contracts remove the need for meter churn when a consumer changes retailer? Does this cause any unforeseen difficulties or create any material risk?</i></p> <p><i>Are there any alternative approaches to reducing the need for meter churn?</i></p>	<p>Where the retailer (rather than the Local Network Service Provider (LNSP)) is the Meter Provider then when a customer churns retailer, the new retailer may remove the existing meter and install their own.</p> <p>The Draft Report proposes that meter churn associated with retailer churn could be addressed if:</p> <ul style="list-style-type: none"> retailers (where they are the Meter Provider) are required to provide customers with separate contracts for energy and metering; or the customer contracts directly with the Meter Provider. <p>The Businesses consider that both of the proposed approaches require further consideration. In particular, in relation to the second proposed approach:</p> <ul style="list-style-type: none"> accuracy and maintenance of the meter would rest with the customer. This raises various customer protection issues and would require that customers are well educated about meters and who the accredited meter providers are; and the Responsible Person role under Chapter 7 of the Rules would be split into two roles – one relating to the Meter Provider and another relating to the Meter Data Provider. Accordingly, the benefits of having a single Responsible Person, which underpinned the AEMC Rule determination on this matter, would be lost. <p>This problem has been avoided in Victoria as the DNSP has been nominated the exclusive meter provider of AMI meters. The benefits of this approach are widely documented, including in cost benefit analysis undertaken for the SCER in 2008⁶.</p> <p>Other possible arrangements to avoid meter churn resulting from retailer churn include meter leasing arrangement or franchise metering areas. These approaches are not considered in the Draft Report.</p>
10.	<p><i>Are there sufficient potential metering services providers to facilitate a contestable roll out of AMI? Does the proposed model mitigate all the material risks of a contestable roll out? If not, should a monopoly roll out be adopted?</i></p>	<p>In Victoria, the Victorian Government mandated an accelerated DNSP led AMI roll out based on the findings and recommendations of an independent cost-benefit study, which assessed the expected net-benefit to consumers of a mandated DNSP led roll-out.</p> <p>This roll-out is currently progressing well and will provide a technology platform which will deliver a multitude of benefits and opportunities for Victorian consumers. Some of these benefits and opportunities are available now and others benefits will progressively be made available beyond the completion of the AMI rollout. These benefits, arising from a range of products and services, include</p>

⁶ Found at: http://www.ret.gov.au/Documents/mce/_documents/RIS_Phase2_Smart_Meters_Jurisdictional_and_Detailed_Analysis20080408120346.pdf

		<p>better information via internet portals and in-home displays, automatic fault detection and faster outage response, remote meter reads, elimination of estimated meter reads, remote connection and disconnection, remote meter condition monitoring, network condition monitoring and flexible pricing.</p> <p>Under the Victorian mandated AMI roll-out, it will take around five years for the roll-out to be completed and longer again to achieve comprehensive introduction and take-up of the benefits and opportunities created by AMI. Any future non-mandated roll-outs of smart meters are likely to take far longer and will depend on the level of acceptance of smart meters from consumers and stakeholders.</p> <p>The deployment of smart meters requires the close coordination and cooperation between multiple industry participants, stakeholders and consumers as the impact on different groups will vary - this inevitably leads to different levels of cooperation and different timing of investments by various parties. Notwithstanding, the benefits can only be realised, to their full extent, when there is investment in new technology, IT systems, new business processes and detailed stakeholder communication.</p> <p>To this end, it is questionable whether the benefits and opportunities created by smart meters would ever be realised under a non-mandated roll-out.</p> <p>The Businesses therefore continue to support a mandated and accelerated roll-out approach to smart meters for the same reasons as set out in the cost-benefit analysis of options for a National Smart Meter Roll-Out, undertaken for SCER in 2008 (the then MCE). This analysis concluded that:</p> <p><i>Providing for a mandated roll-out by one party (rather than more complicated fundamental changes to the regulatory framework) is seen as the preferred approach to facilitating a roll-out of smart meters⁷.</i></p> <p>It further stated that in terms of a non-mandated and accelerated approach, referred to a “new and replacement approach”:</p> <p><i>It would be more expensive, including in the areas of installation, communications and other back-end systems. In addition, a new and replacement approach would take many years to reach the majority of users. Without dense coverage of smart meters, most benefits will not be achieved.</i></p> <p>The cost-benefit analysis estimated that a roll-out led by DNSPs would result in the greatest potential net benefits amongst the four scenarios examined and noted that that the benefits from a DNSP led smart meter roll-out are largely due to a wider range of communications options and synergies with network management. The cost-benefit analysis also estimated the largest proportion of smart meter benefits are achieved through operational efficiencies in the DNSP.</p> <p>On this basis the SCER issued a Statement of Policy Principles, in accordance with clause 4.4(a) of</p>
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⁷ Found at: http://www.ret.gov.au/Documents/mce/_documents/Smart_Meter_Decision_Paper_MCE_13_June_200820080613153900.pdf

⁸ Found at: http://www.ret.gov.au/Documents/mce/_documents/MCE_Statement_of_Policy_Principles20080613154127.pdf

		<p>the Australian Energy Market Agreement (AEMA) and s. 8 of the NEL, which states that⁸:</p> <p><i>To maximise the net benefits of a mandated roll-out of smart meters in a timely manner and capture the operational benefits for distribution network service providers, distribution network service providers will be legislatively obliged to roll out smart meters to some or all residential and other small customers in those jurisdictions where a mandated roll-out will take place.</i></p> <p>The Businesses consider that, any change to this policy position should be the subject of a full Regulatory Impact Assessment to ensure consistency with the NEO and it should also be tested for practicability.</p>
11.	<p><i>What should the exit fee when a consumer upgrades its meter from one provided by the local distribution business? Is the proposed fixed 30% of the cost of a replaced meter appropriate?</i></p>	<p>In Victoria, at the end of the mandated AMI roll out period, there will be some small customers who have not been upgraded to an AMI meter for a variety of reasons. The Businesses note that these customers should be required to pay an exit fee when they eventually transfer to an AMI meter and that this should:</p> <ul style="list-style-type: none"> • ensure that Victorian DNSPs recover their full cost of providing the existing meter; and • be recovered from the individual customer incurring the costs, on the basis that it is a directly attributable cost. <p>The Businesses do not support the AEMC's proposal that the exit fee is fixed at 30 per cent of the cost of a replaced meter. The exit fee should be calculated separately for each DNSP to ensure that they recover their full fixed and variable costs associated with the meter installation and any other associated costs.</p> <p>Under the Victorian Cost Recovery OIC, the exit fee arises when the DNSPs AMI meter is removed and the retailer takes over the responsibility for metering services. The exit fee is intended to fully recompense the DNSP for the fixed and variable costs it has and would incur for the metering installation which is no longer required. This includes the meter, the communications infrastructure and IT support systems. The OIC allows the DNSP to determine this charge to ensure full cost recovery of the investment required under the Government mandated roll out.</p> <p>This is consistent with the SCER's Statement of Policy Principles which provides that⁹:</p> <p><i>The regulatory framework for distribution network tariffs, consistent with the revenue and pricing principles, should ensure that distribution network service providers:</i></p> <ol style="list-style-type: none"> a. <i>are able to recover in a transparent manner the costs directly resulting from meeting the mandated service standards for smart meters and the costs of their existing investment which has been stranded by any mandatory roll out.</i>

⁹ Found at: http://www.ret.gov.au/Documents/mce/_documents/MCE_Statement_of_Policy_Principles20080613154127.pdf

12.	<p><i>Does the option of a government mandating an AMI roll out within its jurisdiction act as a strong disincentive to a commercial roll out? Should the ability for these governments to mandate an AMI roll out be removed from the NEL?</i></p>	<p>Refer to the Businesses' response to question 10.</p>
<p>Chapter 5: Demand side participation in wholesale electricity and ancillary services markets</p>		
<p><i>Demand response mechanism</i></p>		
13.	<p><i>Participation in the wholesale market:</i></p> <p>(a) <i>Do stakeholders agree that the proposed demand response mechanism is likely to result in efficient consumption decisions by end-users? If not, are there any changes you recommend to the mechanism to facilitate this?</i></p> <p>(b) <i>On balance, is a new sub-category of market generator required for consumers providing a demand that enables aggregation? What types of issues should be considered when developing the registration process?</i></p>	<p>The Businesses support the concept of consumers, or third parties acting on behalf of consumers, participating in the wholesale market by providing “negative load” (i.e. reduction in consumption). Under the proposed approach consumers would be paid the prevailing spot price for providing “negative load”. This would result in this form of demand side management being treated in the same way as generation capacity.</p> <p>This would be a significant change to the structure of the NEM and would require changes to many aspects of the legislative and regulatory framework, including AEMO’s dispatch process, to ensure the stability of the market (including voltage control) and protection of consumers. To this end, the Businesses consider an industry working group should be established to ensure all issues are identified and appropriately addressed.</p>
14.	<p><i>Consumer baseline consumption:</i></p> <p>(c) <i>What factors should be taken into consideration when developing a baseline consumption method?</i></p> <p>(d) <i>Have we identified the correct three key principles for developing a baseline consumption method (data refresh, accuracy, metering)?</i></p> <p><i>Are there any substantial changes to metering and settlement arrangements required for this mechanism to be implemented? Can these issues be resolved through AEMO’s consultation process and procedures or are broader amendments to the rules required?</i></p>	<p>The Businesses agree with the Draft Report that given the complexity of developing a suitable method for calculating baseline consumption, it would be best addressed through an industry working group.</p>
15.	<p><i>Incorporating demand response into central dispatch:</i></p> <p>(e) <i>Do you agree that similar arrangements for generation should apply to demand resources in terms of thresholds</i></p>	<p>In the limited time available to file a submission, the Businesses have not fully considered this issue and would therefore welcome the opportunity to participate in further consultation on this matter.</p>

	<p><i>for registering as scheduled or non-scheduled basis?</i></p> <p>(f) <i>What are the ways in which the regulatory arrangements can be adapted to facilitate the participation of scheduled and non-scheduled load in AEMO's central dispatch process? Are there any specific changes to reporting, telemetry and communication requirements?</i></p> <p>(g) <i>Should both market and non-market loads above a certain size be required to provide information to AEMO regarding their controllable (and therefore interruptible) load blocks?</i></p> <p>(h) <i>Should there be a trigger in the monitoring and reporting framework that requires consumers to provide greater detail regarding their demand resource to AEMO or affected DNSPs?</i></p>	
Demand forecasting		
16.	<p><i>How should AEMO's powers be expanded to improve demand forecasting? Should retailers and other market participants be obliged to provide information regarding DSP capabilities? Will non-obligatory requirements achieve the desired accuracy in reporting requirements?</i></p>	<p>A key role for AEMO, as the electricity market operator, is ensuring that supply and demand are balanced in the NEM. To this end, AEMO prepares demand and energy forecasts at an aggregate level for each state. It is understood that AEMO has limited ability to take into account energy efficiency initiatives in developing these forecasts.</p> <p>DNSPs also prepare demand forecasts for their distribution areas, which have regard for energy efficiency initiatives. These forecasts also incorporate DSP to the extent this is reflected in existing demand.</p> <p>The Businesses consider AEMO should have greater regard for the impact of energy efficiency initiatives in developing its demand forecasts, however this does not require any change to its current powers.</p> <p>The Businesses emphasise that demand forecasts play a key role in identifying areas where there would be benefit in pursuing future DSP initiatives.</p>
17.	<p><i>In what ways can AEMO improve its survey questions regarding DSP capabilities? How often should AEMO be required to update its expectations on DSP capabilities in the NEM?</i></p>	No comment.
18.	<p><i>Would a pre-dispatch that includes active and price-responsive DSP improve decision making processes for C&I users and aggregators? If not, do you have any other suggestions for</i></p>	No comment.

	<i>improving the ability for AEMO to accurately forecast demand?</i>	
Creating new category of market participant		
19.	<i>Do you agree that a new category of market participant should be established for the provision of non-energy services?</i>	No comment.
20.	<i>What types of issues should be considered when developing the registration process, such as eligibility, obligations and liabilities?</i>	
21.	<i>What metering arrangements need to change to implement this mechanism?</i>	
Chapter 6: Efficient and flexible pricing options		
Phasing in time varying pricing		
22.	<i>Do stakeholders agree with our approach for phasing in cost-reflective pricing? If not, how can the policy be improved to transition to cost-reflective pricing?</i>	<p>On 25 September 2012, the Victorian Government announced the introduction of “flexible tariffs” (also known as time of use (ToU) tariffs) in Victoria from mid 2013. Key features of the Victorian Government’s “flexible tariff” initiative include that:</p> <ul style="list-style-type: none"> • DNSPs must offer retailers a flexible network tariff for residential customers (less than 160 MWh per annum) as well as existing legacy network tariffs (those tariffs customers are on when flexible pricing is introduced); • flexible network tariffs based on a ‘common form’ structure comprising a peak, off peak and shoulder component; • customers must choose to “opt-in” to a flexible network tariff - consumer must have AMI meter installed in order to “opt-in”; and • customers can revert to their legacy tariff or move to a new flat rate tariff at no cost until March 2015. <p>The Businesses welcome the Victorian Government’s initiative for flexible tariffs, which effectively removes its existing moratorium on ToU tariffs. Allowing DNSPs to introduce cost reflective tariffs is key to encouraging the efficient use of the network. They therefore encourage consumers to use electricity at times when there is lower demand, thereby reducing peak demand and the need for investment in infrastructure.</p> <p>Importantly, the approach proposed in the Draft Report, is different to that introduced by the Victorian Government, as it provides a gradual phasing in of “time varying network tariffs” (i.e. also known as “flexible tariffs” or ToU tariffs) on the following basis:</p> <ul style="list-style-type: none"> • Band 1 – large load customers - will be mandatorily assigned to “time varying network tariff” with

		<p>no option for a flat tariff;</p> <ul style="list-style-type: none"> • Band 2 - medium to large residential and small business customers – will be deemed to be on a “time varying network tariff” however may choose to “opt-out” and move to a flat network tariff; and • Band 3 - small to medium residential and small business customers – will be deemed to be on a flat network tariff, however may choose to “opt-in” to a “time varying network tariff”. <p>Band 1 to 3 customers relate to residential and small business customers whose consumption is less than 100Mwh per annum (as defined under the National Energy Retail Law (NERL)). Again, retailers are free to choose how to include the relevant network tariff into their retail offers.</p> <p>The Businesses support the AEMC’s approach, subject to the amendments outlined in the Businesses’ response to question 24, including removing the consumption thresholds and deeming all small customers to be on “time varying network tariffs”.</p> <p>It is unclear, however, how the approach proposed in the Draft Report is intended to accommodate jurisdictional initiatives such as the Victorian Government’s flexible tariff approach or ToU pricing in NSW. The Businesses note that the Victorian Government has indicated that it will review its flexible pricing initiative at the end of 2015 to determine whether to continue, amend or transition to the national approach.</p>
23.	<p><i>Have we identified the main issues with transitioning to cost reflective pricing? If not, what other issues need to be considered?</i></p>	<p>As discussed in response to question 22, any future national cost reflective tariff framework should have regard for, and accommodate, differences in existing jurisdictional arrangements.</p> <p>It is unclear how the framework set out in the Draft Report intends to accommodate the Victorian Government’s “flexible tariff” initiative. The Businesses consider this is an important issue and welcomes the opportunity to discuss this with the AEMC together with the Victorian Government.</p> <p>The Businesses also note the following transitional issues:</p> <ul style="list-style-type: none"> • DNSPs should have flexibility to develop their own “time varying network tariff” structure, having regard for their specific load profile and customer base, in order to recover their costs and manage peak demand subject to satisfying the pricing principles under the Rules. The structure of any future “time varying network tariff” should not be prescribed in the Rules; • any changes to network tariffs should be for a minimum period of 12 months. This is consistent with the DNSPs annual pricing cycle, which involves DNSPs developing their annual tariff strategy for approval by the Australian Energy Regulator (AER). This is important to assist DNSPs manage risk associated with customers reverting from “time varying network tariff” to legacy network tariffs. The AEMC acknowledges that “the introduction of “time varying network tariffs creates new risk that will need to be managed”. Typically businesses manage risk through

		<p>a combination of insurance, hedging contracts and price offerings to their customers. DNSP rely mainly on prices as a risk management tool – however, the effectiveness of this is limited to the annual cycle under which they can introduce changes to their tariff rates and structures. Retailers, however, are unconstrained in their ability to use pricing as a risk management tool – they are able to change prices on a daily basis. When finalising its recommendations on this matter, the Businesses strongly encourage the AEMC to have regard for the difference in DNSPs and retailers ability to manage their risk through tariffs; and</p> <ul style="list-style-type: none"> • once customers have transitioned to cost reflective pricing they should not be able to revert back to their flat network legacy tariff (those tariffs customers are on when flexible pricing is introduced), albeit new flat retail tariffs will be available. Maintaining legacy network tariffs for customers to revert back to, is costly for the industry and should not be necessary from a customers perspective if the introduction of new tariff offerings are appropriately supported. This would involve consumer information, communication and engagement campaigns and programs to ensure consumers are informed about new pricing options. In particular: <ul style="list-style-type: none"> ○ consumers must have a smart meter and should understand the core and additional functionality available to them; ○ the network tariff should be “unbundled” from the retailer’s tariff and displayed on consumers’ electricity bills, issued by the retailer. This will increase transparency of how the final bill is developed and therefore assist consumers to better understand how their usage impacts their final bill; ○ consumers must understand their consumption data and understand their usage patterns; ○ consumers must have access to independent price comparison tools so they can navigate the energy market in an informed way; and ○ flexible pricing structures their impacts should be clearly explained, particularly to vulnerable consumer groups.
24.	<i>How should consumption thresholds be determined?</i>	<p>Under the Victorian Government’s “flexible tariff” initiative all residential customers can voluntarily elect to have a “flexible tariff”.</p> <p>Studies indicate that the uptake of “flexible tariffs” under an “opt-in” approach will be much lower than under an “opt-out” approach where all customers are deemed to be on flexible tariffs unless they “opt-out” (i.e the band 2 approach as set out in the Draft Report). Therefore, the benefits arising from cost reflective pricing will likely be much lower under the Victorian Government’s flexible pricing initiative than under the AEMC’s proposed approach, which is based on a combination of approaches including mandatory reassignment, opt-out and opt-in as defined by three consumption thresholds that are yet to be determined. The Draft Report proposes that jurisdictions will be able to determine their own</p>

		<p>consumptions thresholds.</p> <p>While the AEMC’s proposed approach is likely to result in a greater number of customers on cost reflective tariffs, the three band approach is overly complex and unnecessary.</p> <p>The Businesses:</p> <ul style="list-style-type: none"> • suggest removing the consumptions thresholds and deeming all small customers to be on cost reflective tariffs would provide a far more coordinated approach. Retaining the consumptions thresholds as proposed in the Draft Report may result in customers in the same threshold consumption bands potentially being treated differently depending on rollout option adopted in their jurisdiction. Further, allowing each jurisdiction to determine its own consumption thresholds may be complex for national retailers to manage; and • emphasise that deeming all small customers to be on cost reflective tariffs will not prevent customers from electing a flat rate tariff from their retailer. As would be expected, in a competitive environment, retailers will offer a variety of tariff options including flat tariffs to meet consumers’ demands. As noted above, under both the Victorian Government’s and the AEMC’s proposed approaches, retailers are free to choose how to include the relevant network tariff into their retail offers. <p>Further, the Businesses expect that there will be adequate consumer education, provided by Government, retailers and customer groups, on tariffs so that consumers fully understand the impact of any changes to their existing tariff structure.</p>
<p>Phasing in time varying pricing</p>		
<p>25.</p>	<p><i>We seek stakeholder comments on appropriate pricing principles for distribution businesses and the appropriate time period for stakeholder consultation on distribution network pricing proposals.</i></p>	<p>The Draft Report proposes to amend the pricing principles set out in clause 6.18.5 of Chapter 6 of the Rules to “strengthen the guidance” on the introduction of “time varying network tariffs”. In particular, to address any concerns that DNSPs may “shift costs from responsive to unresponsive consumers [such that] those consumers on flat retail tariffs could therefore see significant increases in their tariffs”. The Draft report also proposes that DNSPs should be required to consult with external stakeholders on their network tariff structures in their annual pricing proposal.</p> <p>The Businesses submit that:</p> <ul style="list-style-type: none"> • currently, the pricing principles require that DNSPs’ tariffs are cost-reflective, free from cross-subsidy, equitable, simple and efficient. They also require DNSPs to take into account the long run marginal cost (LRMC) for the service when developing their tariffs. While they do not require DNSPs tariffs to signal the time varying nature of network costs they are sufficiently flexible to accommodate such tariffs as well as other types of cost reflective tariffs that may assist in promoting the efficient use of the network including:

		<ul style="list-style-type: none"> ○ capacity / volume based tariffs; and ○ dynamic or critical peak pricing tariffs. <p>This is evidenced by NSW DNSPs who have been offering ToU tariffs for many years now under the existing pricing principles – the AER has annually approved these tariffs as being consistent with the existing pricing principles. Further, the Businesses emphasise that, consistent with the Victorian government’s recent flexible pricing initiative, they can and will introduce flexible pricing under the current pricing principles.</p> <p>Further, the Businesses emphasise that the only reason why they have to date not introduced ToU tariffs is because of the Victorian Government’s moratorium on the introduction of these tariffs.</p> <p>To this end, increasing prescription in the pricing principles will only act to reduce flexibility for DNSPs to develop innovative and efficient network tariffs relevant to their own circumstances (that reflect the nature of their customer base) and preferences.</p> <ul style="list-style-type: none"> • they already consult with extensively with both Government and retailers.
Chapter 7: Distribution networks and distributed generation		
<i>Potential return for network businesses implementing DSP projects</i>		
26.	<p><i>Would it be beneficial to include reference to the suggested mechanisms and provide more guidance and an overall objective in the Rules governing the demand management incentive scheme?</i></p>	<p>The AEMC acknowledges that that currently the only incentive scheme relating to demand side management (DSM) is the DMEGCIS (in Victoria this is referred to as the DMIS). While the AER has discretion under the rules to develop a capex efficiency benefit sharing scheme (capex EBSS) that could incentivise DSM activities, it has to date chosen not to develop such a scheme. This issue is, however, currently being reviewed as part of the Economic Regulation Rule Change.</p> <p>To address the concerns that the incentives under the DMEGCIS are weak, the Draft Report proposes a number of potential changes that could be incorporated into Chapter 6 of the Rules to strengthen the current incentives under the DMEGCIS or potentially a capex EBSS. The Businesses strongly support these changes which include:</p> <ul style="list-style-type: none"> • allowing expenditure associated with projects approved under DMEGCIS to be treated in the same manner as all other operating and capital expenditure; • allowing DNSPs to retain the value of capex savings resulting from the implementation of a DSP project. This would require that : <ul style="list-style-type: none"> ○ the DSP project has removed or deferred the need for capital investment; and ○ the approved cost of the capital investment can be identified by the AER. • Allowing DNSPs to earn a share of market benefits, arising from investment in DSP, that accrue

		<p>to the other sectors of the supply chain. The Draft Report suggests that method for calculating benefits across the supply chain is a matter for the AER to determine;</p> <ul style="list-style-type: none"> • Allowing DNSPs to recover foregone revenue from implementation of DSP including DSP tariff based projects; • Criteria, to be included in the Rules, which would guide any future DMEGCIS developed by the AER. The proposed criteria include: <ul style="list-style-type: none"> (i) DSP project must be efficient – as determined by the AER; (ii) payment of reward should reflect timing of benefits in order to smooth the bill impact on consumers; (iii) costs associated with the value that would have occurred if the customer has used the electricity at that time (lost consumer benefit), must also be included in the assessment. (iv) the value of the share of market benefits should be capped (v) the rewards should be calibrated with regard to the value of the non network benefits which can be passed through to consumers (vi) the longer term value of DSP activities beyond the regulatory period in which the activities are undertaken should be recognised (vii) have regard to other incentive schemes being applied to the Businesses (viii) projects approved under this scheme should undergo the same cost approval process as all capital or operating expenditure and (ix) an underlying network issue is being addressed by the DSP project <p>The AEMC further proposes that any future incentive schemes which support the above proposed changes should be developed in consultation between the AER and the network businesses. The Businesses strongly support this proposal.</p>
27.	<p><i>Should separate provisions for an innovation allowance be included into the rules? Given that the costs of the allowance would be borne by electricity consumers, is it more appropriate for such innovation to be funded through government programs?</i></p>	<p>The Businesses strongly support the regulatory regime incorporating greater incentives for DNSPs to invest in innovative solutions for the provision of distribution services. Promoting and funding innovation is likely to be the most effective long term means of putting sustained downward pressure on network prices.</p> <p>The Businesses agree that the innovation requirements would be better addressed separately from the DMIS in the Rules. In particular, the Rules could include high level principles to guide the AER's development of an innovation incentive scheme. The Businesses highlight that the UK regulatory framework, "Revenue using Incentives to deliver Innovation and Outputs" (RIIO), places a strong emphasis on innovation recognising that this will lead to lower prices and improved investment over the</p>

		longer term.
Possible application to the transmission network business		
28.	<i>Should the provisions for a demand management incentive scheme be included in the regulatory framework for transmission businesses?</i>	No comment.
Network tariff structure influencing incentive to do DSP		
29.	<i>What amendments are required to the current distribution pricing principles as set out in clause 6.18.4 of the national electricity rules to incentivise DNSPs to undertake DSP?</i>	<p>The Draft Report proposes amendments to the distribution pricing principles as set out in clause 6.18.4 of the Rules, which govern assignment or re-assignment of retail customers to tariff classes. The AEMC is concerned that network tariffs are not designed to be cost reflective but rather to maximise volumes and that as a result volumes are linked to profits rather than efficient costs.</p> <p>The Draft Report also proposes greater involvement from the AER in the annual tariff setting process. In particular, it states “the AER should be checking and encouraging distribution businesses to actively develop and improve their tariff structures to meet the defined principles”.</p> <p>As noted in the Businesses’ response to question 25, the Businesses do not consider that any changes are required to the pricing principles at this time.</p> <p>In Victoria, the roll out of AMI meters and the removal of the Victorian Government’s moratorium on the introduction of flexible tariffs, will allow DNPs to introduce more cost reflective pricing. The Businesses also support expanding provisions relating to the recovery of foregone revenue, to include foregone revenue relating DSP tariff based projects. This will also assist to ensure that profits are linked to the efficient costs of investment, rather than volumes.</p>
Providing clarity and flexibility for DSP related expenditure		
<i>The AEMC seeks stakeholders views on the following proposed Rule amendments:</i>		
30.	<i>Clarify that the AER can consider market benefits when assessing efficiency of network expenditure allowances</i>	<p>The Businesses support this recommendation which clarifies that DNSPs can include non-network DSP solutions in their capex forecast, submitted to the AER for approval as part of their building block proposal during a regulatory rest. It is understood that the DSP solution must be addressing an underlying network issue and therefore deliver some network benefits.</p> <p>The Businesses note that, if adopted, this change would result in greater alignment between the capex expenditure criteria under Rules with requirements under RIT-D.</p>
31.	<i>Include flexibility to address any extra volatility in DSP expenditure.</i>	The Businesses support this recommendation which addresses industry concerns that some DSP solutions, such as peak time rebate, are more uncertain in terms of when the DNSP will incur the costs compared to capital infrastructure investments.

		The Businesses agree that the AER should fully consult with DNSPs in developing this provision.
32.	<i>Provide more certainty on how unforeseen DSP costs are treated and allowed for at the next regulatory control period (137)</i>	<p>The Businesses support the recommendation that a new rule, based on clause 6A.6.6 of the Rules, is incorporated into Chapter 6 of the Rules. Clause 6A.6.6 provides that:</p> <p><i>the AER must accept the forecast of required operating expenditure of the Transmission Network Service Provider included in a Revenue Proposal in relation to the remainder of costs required to meet obligations under the relevant agreement for network support services in the relevant regulatory control period.</i></p> <p>This would provide greater certainty for DNSPs that costs associated with a network support agreement that crosses regulatory control periods, would be accepted as allowed operating expenditure in the upcoming regulatory control period. The Businesses consider that this should be broader than just network support payments and should relate to DSP costs more generally.</p>
33.	<i>Temporary exemption from the STPIS</i>	<p>The Businesses support the recommendation to provide DNSPs with temporary exemption from the service target performance incentive scheme (STPIS) for specific DSP trials and pilots. The Businesses consider, however, that this exemption should be broader than pilots and trials because DNSPs are responsible for the s-factor liability arising from any non-performance of a non-network solutions even where they are not the proponent of the DSP initiative. DNSPs naturally seek to avoid any such liability under the STPIS. Extending the exemption from the STPIS will likely increase the investment in DSP where it is efficient to do so and would result in a net benefit for consumers.</p>
<i>Distributed generation</i>		
34.	<i>The Draft Report proposes a number of recommendations and proposals in relation to distributed generation (DG) and seeks stakeholders views on these</i>	<p>The Draft Report:</p> <ul style="list-style-type: none"> concludes that “there is no need for the introduction of a specific incentive payment mechanism – like the Ofgem model - to incentivise DNSPs to facilitate the connection and export of power from DG”; notes that the potential for a “fee for service” provided by DNSPs to DG proponents to assist them in developing their connection inquiries and applications is being considered by the AEMC as part of the ClimateWorks Australia, Seed Advisory and the Property Council Rule change proposal (ClimateWorks Rule change proposal); recommends that AER should give consideration to the benefits of allowing DNSPs to own and operate DG assets when developing the national ring fencing guidelines. recommends that SCER should, in developing the national approach to feed in tariffs, encourage owners of DG to maximise the export of their energy during peak demand periods. <p>The Businesses submit that:</p>

		<ul style="list-style-type: none">• they continue to support the introduction of a specific incentive payment mechanism – like the Ofgem model – to incentivise DNSPs to facilitate the connection and export of power from DG for the same reasons as set out in their submission on the Directions Paper;• they have presented their views on the benefit of a fee for service” provided by DNSPs in their submission on the ClimateWorks Rule change proposal. The Businesses support this proposal;• they strongly support the recommendation to allow DNSPs to own and operate DG assets and consider that these investments will assist in network support; and• they continue to support the approach to feed in tariffs as set out in their submission on the Directions Paper, which is based on market-based gross metered pricing. The Businesses note that the SCER is currently developing guidelines for a consistent national approach to feed in tariffs and would welcome the opportunity to comment on draft guidelines.
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