

Mr Neil Howes
Senior Adviser
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Project Reference ERC0209

6 June 2017

Lodged online

Dear Mr. Howes

Draft Rule Determination – Replacement Expenditure Planning Arrangements

The Australian Energy Council (the AEC) welcomes the opportunity to make a submission to the Australian Energy Market Commission (AEMC) on the Draft rule determination – Replacement Expenditure Planning Arrangements.

The Australian Energy Council is an industry body representing 21 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia, and sell gas and electricity to over 10 million homes and businesses.

Non-network solutions

The Australian Energy Regulator (AER) has proposed its replacement expenditure rule change request in the context of emerging technology changes. These changes suggest that non-network solutions are becoming more viable alternatives to replacement network investment.¹

Non-network solutions will certainly be viable alternatives in some network replacement projects in the coming decade. Whilst they may not make up the majority of replacement network investment in that time they will continue to grow as technologies become more available and their costs come down. The policy and regulatory settings for replacement expenditure planning arrangements will influence both the development of a dynamic market in the supply of non-network solutions, and will also assist to optimise efficiencies from the continued uptake of small scale systems. The National Electricity Objective is also enhanced through the extension of effective competition into more services as enabling technologies evolve.

In this context competition, where practical is the best mechanism for providing network and non-network services to customers at an efficient cost and to drive innovation, with regulated monopoly DNSPs a second-best approach. Competition seems a very practical approach to adopt for opex funded non-network solutions.

¹ AEMC Replacement expenditure planning arrangements, Draft rule determination, 11 April 2017, Sydney

Regulatory Investment Test

The AEC is the proponent for a suite of rule changes currently under Australian Energy Market Commission (AEMC) consultation². These rule changes clearly intersect and overlay with the AEMC's consultation on the draft rule determination on Replacement Expenditure Planning Arrangements. Part of the AEC rule change is changes to the Regulatory Investment Tests (RIT) to ensure competitive non-network solutions are considered for the widest practicable range of investment decisions. This includes addressing the current RIT financial thresholds, as the high threshold value of the RIT–D, when applied in addressing (or not addressing) both network peak and energy peak, compromises both allocative efficiency and dynamic efficiency³.

Competitive neutrality

To be truly effective that the rules framework needs to reinforce competitive neutrality, i.e. maximise the scope for independent competitive providers to supply network support services to networks. Work remains to be done to lower the financial thresholds applicable to replacement expenditure to ensure the widest penetration of lowest cost solutions practicable.

A range of regulatory tools are related to this and should be considered as being in scope in this regard, including:

- Legal separation of unregulated affiliates and strong ring-fencing;⁴
- Cost allocation guidelines;
- The inadequacy of the current DAPR, and better information provision of where on the network support services may have most value⁵; and,
- Access to cost-reflective tariffs.

Close examination of the incentive schemes such as the Demand Management Incentive Scheme (DMIS) and the Efficiency Benefits Sharing Scheme (EBSS)⁶ is also important to the integrity of policy and regulatory settings for replacement expenditure planning arrangements, in particular to ensure these schemes cannot be substituted by DNSPs for non-network replacement expenditure.

The AEC broadly support the draft rule, recognising that it represents part of a broad-ranging suite of reforms.

² Amendments to Chapters 5, 6, 6A and 7 of the National Electricity Rules in the Implementation of Demand Response and Network Support Services, Australian Energy Council, October 2016

³ The AEC Contestability of Energy Services rule change proposes that the threshold must be reduced from \$5 million for distribution network investments to \$50,000

⁴ AER Ring Fencing Guideline Final Decision, November 2016

⁵ AER Consultation on the Draft Annual Planning Report Template, May 2017, is currently reviewing these

⁶ AER Demand Management Incentive Scheme and Innovation Allowance Mechanism consultation is currently open.

Should you have any questions in relation to this rule change request please contact David Markham, telephone 03 9205 3107 or at david.markham@energycouncil.com.au

Yours sincerely

A handwritten signature in blue ink, appearing to read 'S. McNamara', with a long horizontal flourish extending to the right.

Sarah McNamara
General Manager Corporate Affairs