

**A submission by Tasmanian officials in response
to the discussion paper presented by the
Australian Energy Market Commission
on 1 April 2011 entitled:**

Strategic Priorities for Energy Market Development

Prologue

The Tasmanian Office of Energy Planning and Conservation (OEPC) congratulates the Australian Energy Market Commission (AEMC) for the work that has done so far, and welcomes the opportunity to provide feedback on the discussion paper presented to a meeting of stakeholders at Tullamarine on 1 April 2011.

The comments in this submission are from the Director and staff of the OEPC in the Tasmanian Department of Infrastructure Energy and Resources.

The comments do not constitute a submission from the Tasmanian Government. However, the comments are provided in the context of existing Tasmanian policies and positions.

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Key Points

The Tasmanian Office of Energy Planning and Conservation (OEPC) supports the strategic priorities set out on page 6 of the AEMC discussion paper, and elaborated in Chapters 3, 4 and 5. However, we suggest that there is merit in clarifying the underlying objectives, rearranging the strategic priorities and elaborating on some aspects.

There are many ways to categorise and articulate objectives, priorities and strategies. Semantic differences should not become a distraction to this important exercise. The key concern is to build agreement on the objectives and develop a shared sense of what needs to receive more focus or be done differently.

The objectives should provide context and direction for the AEMC's work and be useful to the AEMC for prioritising what it does, and how it does it. Likewise the strategic priorities need to be clear about what they are trying to achieve. To that end we would like to offer some views and suggestions.

Firstly we suggest that it would be useful to be clear about which objectives are within the scope of the National Energy Market (NEM) and its institutions, and those that are not or which lie somewhere in between. This guides the possible courses of action open to the AEMC.

Agreed priorities that are within scope of the National Energy Market (NEM) and its institutions are amenable to self-initiated action by the AEMC and NEM stakeholders.

Matters which are not fully within the scope of NEM stakeholders require a different approach. For example, the current considerable uncertainty linked to climate change issues is not something the AEMC can fix by itself, but it is something that the AEMC and NEM stakeholders can recognise, mitigate and try to influence.

The first of the strategic priorities suggested by the AEMC discussion paper is centred on maintaining the regulatory and market environment for rewarding economically efficient investment. The second focuses on flexible demand measures and the third focuses on ensuring that the transmission framework delivers efficient and timely investment.

The OEPC suggests these priorities might benefit from being clarified, rearranged and augmented along the following lines:

1. **Ensuring adequate investment and an efficient supply chain.** There is a need for ongoing and careful consideration of every part of the energy supply chain – generation, transmission, distribution, retailing and demand side participation – and the AEMC is already doing this. Adequate and efficient investment must remain a strategic priority.
2. **Additional focus and priority on the issue of peak load growth and other cost pressures that are the driving up prices.** This incorporates the AEMC’s identified priorities related to flexible demand and smart meters, but goes further. There is a major market failure at the moment related to the lack of cost reflective pricing or other controls on loads which add to peak demand growth. An enormous amount of expensive infrastructure is being built to supply electricity for very short periods of time. The current rate of price increases demands a higher priority response by the AEMC and other NEM stakeholders.
3. **Additional focus and priority on achieving secure, reliable national electricity supply with a much lower average emissions intensity.** One way or another, Australia is going to need a lot more electricity generation that is cleaner than conventional coal based generation. The size of the task is enormous, the time pressure considerable and the risks are significant. There a lot that the AEMC and NEM stakeholders more generally can do to help ensure that this major transformation occurs in a timely, sensible and economically efficient manner.

The OEPC suggests that these three areas should become the strategic priorities for the AEMC. The transmission issues raised by the AEMC discussion paper can be incorporated into the three areas listed above.

As always there are additional and supporting objectives.

Building **market resilience** is mentioned in the final chapter of the Discussion Paper. This is an important matter and the OEPC suggests that it could be grouped with risk management more generally to form a fourth strategic priority. In addition to financial risks, we have in mind the risks associated with planned and unplanned exits from the supply industry, prolonged uncertainty, underinvestment, skills shortages and so on.

Energy efficiency is mentioned in passing in the second set of priorities articulated by the AEMC. However, the OEPC feels that energy efficiency objectives and strategies are important enough to have a grouping of their own. There a lot that the AEMC and NEM stakeholders can do in energy efficiency that supports the long term interests of energy consumers.

Finally, consideration could be given to having a group of objectives and priorities related to facilitating and deploying **new technologies** that can assist in the achievement of the main objectives. In generation this would cover renewable energy technologies, large scale energy storage and carbon capture and storage. In networks it would cover things like smart grids, direct load controls, embedded generation and electric vehicles. At the consumer end it could consider the possible role of the National Broadband Network or 3G networks in metering and retailing services and “smart homes”. The OEPC believes that the long term interests of customers are also served by actively fostering and facilitating appropriate technological advances, and that this is a valid part of NEM market development.

Additional Comments

Objectives

The National Energy Objective provides an over-arching goal and context, but it is high level and general. A sub layer of more detailed objectives is therefore useful for guiding specific workload priorities.

However, since the next layer of objectives will not be set forth in National Energy Market Rules or Regulations, the AEMC would presumably like some assurances that its strategic priorities have the general support of the Standing Council on Energy and Resources (SCER) and key NEM stakeholders.

This immediately raises the question of scope. Some potential objectives fall wholly within the scope of the SCER, AEMC and other key NEM stakeholders falls only partially within this scope or not at all. There is also the question of consensus. Some objectives will be able to develop a high degree of support and consensus, and some will not. The following table sets out a categorisation of objectives:

Table 1: Four types of objectives

	Within scope of the SCER/AEMC/NEM* etc	Not within the scope of the SCER/AEMC/NEM etc.
General agreement	Category A objectives	Category B objectives
Inadequate agreement	Category C objectives	Category D objectives

** Note: For brevity, let us denote the collective resources of the Ministerial Standing Council on Energy and Resources, the AEMC, AER and AEMO, and key stakeholders in the NEM as **NEM+**.*

Category D objectives are relatively straightforward because they are someone else's responsibility. However, the AEMC and other key stakeholders in the NEM+ can contribute by informing the debates and decisions elsewhere, by providing and explaining relevant aspects of the energy market, and by responding to developments that are not in the long term interests of energy market customers.

An example of a Category D objective might be "improving the scientific and economic assessments of climate change risks". Important though such an objective might be, it is not within the scope of the AEMC and hence is not suitable for becoming an AEMC strategic priority.

Category A objectives are the fertile ground for strategic priorities. They are within the scope of the NEM+ and can attract a degree of agreement and consensus. The AEMC and other participants in NEM+ can focus on prioritising the objectives and address the "how, when, where, who and by how much" aspects of achieving them. The OEPC believes that the challenges presented by increasing peak load growth fall into this category.

Category B and Category C objectives are problematic.

If a Category C objective is important enough then work may be warranted on pushing for greater agreement and consensus amongst NEM participants, thereby lifting it into Category A.

If a Category B objective is important enough, but is not being handled well enough elsewhere, then consideration should be given to either influencing a better outcome elsewhere or being given more responsibility for handling the matter directly.

The OEPC contends that the sum total of State and Federal Policies related to assisting clean energy generation and assisting higher standards of energy efficiency falls somewhere in Categories B and C. There is a mish-mash of initiatives which in total lack clarity, consistency and cost effectiveness. This is not the fault of NEM+ but it has a large impact upon the market and its customers and other stakeholders in terms of costs, uncertainties and missed opportunities.

To some degree the current difficulties are recognised in the AEMC discussion paper and reflected in the three strategic priority areas identified by the AEMC.

However, the OEPC believes that some of the issues deserve additional discussion, debate and focus.

Market Overview and the Key Challenges

The OEPC contends that there are two very large market failures affecting Australia's energy market, plus a number of smaller ones. The pursuit of economic efficiency through well functioning markets requires that such failures be recognised and addressed.

The first of these major market failures is the absence of a price signal on the greenhouse gas externality. Irrespective of the highly politicised arguments about climate change there is a strong scientific, political and public consensus that greenhouse gas emissions might pose significant risks to the planetary biosphere and hence it is prudent that they be curtailed and abated. Even the debate on climate change action is an externality on the NEM because it is associated with enormous uncertainty and detrimental impacts on investment.

What to do about this market failure is a diabolical challenge that falls largely into Categories B and C as discussed earlier. However, some of the objective outcomes fall more closely into Category A.

The objectives that fall into Category A for the NEM+ include the ones that relate to partially offsetting the absence of a price on carbon emissions from fossil fuel electricity generation by creating additional support for electricity generation from cleaner technologies.

This action also has justification in terms of developing new technologies and industries, diversifying risks and increasing the range of options for supply.

Policies such as a market based bonus for clean electricity should not be viewed as a cross subsidy, but rather as an immediate and reasonably cost effective correction to the very large market failure to price the carbon externality. Furthermore, a market based support mechanism for renewable energy is evidently more achievable in Australia than a carbon price or emissions trading scheme. Hence a well designed renewable energy support scheme could well be a valid complementary policy to a carbon price.

The OEPC believes that policies and actions related to support for cleaner electricity generation technologies should attract a greater degree of attention from the NEM+. Not only from the AEMC, but also from the NEM policy makers, and the industry itself.

The second large market failure is the absence of cost reflective price signals to loads which are adding to rising peak demand. Every Megawatt.hour which adds

to peak loads currently attracts a large and largely hidden cross subsidy from other consumers. The absence of effective feedback means that the problem is accelerating, with severe consequences for end user prices. This in turn has negative consequences for disadvantaged sections of Australian society and the cost competitiveness of trade exposed industries.

The issue is raised within the AEMC discussion paper, but perhaps not as clearly as it might be. In some places the discussion paper seems to put the emphasis on encouraging investments to meet the rising peak demand rather than on finding ways to avoid the need for so much expensive extra investment in the first place.

It is understandable that the energy supply industry should tend to focus on supply side solutions, but the goal of the AEMC is to focus on the long term interests of energy consumers. Large increases in prices are not in the best interests of consumers if they are partly unnecessary.

Objectives broader than Economic Efficiency

The National Energy Market's objective, legislation, governance and institutions focus very much on economic efficiency. This is sensible and pragmatic and should be maintained. However, it begs the question of what to do about social and environmental objectives that have a direct bearing on Australia's energy market and the long term interest of its stakeholders.

Should such issues and objectives just be ignored? Should they be put into the too hard basket? Should they only be addressed when they threaten economic efficiency? Or should they be given more explicit recognition and attention?

The OEPC believes that more effort be applied by the AEMC and NEM+ in addressing these sorts of issues and preserving the economic efficiency objective in the process. Ignoring the issues is likely to lead to suboptimal approaches by others that will only cause an undue amount of inefficiency, distress and rectification later on. That is one of the main reasons why we applaud the work that has been done by the AEMC in the lead up to the discussion paper, and also the considerable contributions made by presenters and others at the Tullamarine workshop.
