



1 February 2008

Dr John Tamblyn
Chairman
Australian Energy Market Commission
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Dear Dr Tamblyn,

**Total Environment Centre Proposal:
National Electricity Amendment (Demand Management) Rule 2007**

SP AusNet welcomes the opportunity to make this submission in response to the Rule change proposal from Total Environment Centre (TEC), which relates to demand side management.

As you know, SP AusNet is one of few Australian energy market participants with substantial network facilities in more than one energy sector category. The company owns the Victorian electricity transmission business, one of five electricity distribution businesses in Victoria, and one of three gas distribution businesses in Victoria. As such, SP AusNet is able to comment on demand side management from a number of different perspectives.

SP AusNet is concerned that a key theme in TEC's proposal document is that the existing regulatory arrangements in respect of electricity transmission are biased towards network investment and against non-network solutions. It is clear from the Rules that such a proposition is incorrect. The submission lodged by the Electricity Network Owners Forum (ETNOF) explains in detail the elements of the Rules that require non-network solutions to be considered by TNSPs. SP AusNet fully concurs with ETNOF's submission.

SP AusNet also notes that TEC's claim of bias presupposes that the network planner and the network owner is the same legal entity. In Victoria, however, SP AusNet is the network owner, whilst VENCORP is responsible for:

- procuring bulk shared network services from SP AusNet and other providers;
- providing transmission use of system services to transmission customers (including administering transmission pricing); and
- planning and directing any augmentation of the shared transmission network.

Furthermore, in Victoria the distribution businesses have responsibility for planning and directing the augmentation of the facilities that connect their distribution systems to the shared transmission network. The Victorian distribution businesses publish an annual Transmission Connection Planning Report, in accordance with regulatory arrangements administered presently by the Essential Services Commission, Victoria. The 2007 edition of that report states that¹:

“One of the purposes of this document is to provide information to proponents of non-network solutions (such as embedded generation or demand management) to emerging network constraints. As noted in further detail in Chapter 2 below, the DBs aim to develop their networks and the associated transmission connection assets in a manner that minimises total costs (or maximises net economic benefit). To this end, proponents of non-network solutions to the emerging network constraints identified in this report are encouraged to lodge expressions of interest with the relevant DB(s).”

As a matter of fact, therefore, TEC’s claim of bias cannot logically apply to SP AusNet, the Victorian distributors or VENCORP. It is disappointing that TEC’s Rule change proposal does not provide any comment on the electricity transmission arrangements in Victoria.

SP AusNet is also concerned at the suggestion that the regulatory arrangements provide incentives to over-invest in networks. As owner of a number of diverse energy networks, SP AusNet does not accept that any of the regulatory regimes over-reward network investment. In fact, regulatory decisions on the cost of capital are a potential source of uncertainty for network businesses that could lead to a less stable investment environment. For this reason, in the Chapter 6A rules the Commission sought to provide some certainty to TNSPs that the WACC parameters would not be subject to change unless there is persuasive evidence supporting a change.

More generally, it is noted that Chapter 6A has been designed to balance strong incentives to achieve cost efficiencies (through the ex ante approach to capital expenditure and the application of an efficiency carry over mechanism) and incentives to improve network performance. Given the substantial work undertaken by the Commission in seeking an appropriate balance of incentives, in addition to the work previously undertaken by the ACCC, it would be extremely surprising and concerning if a radical overhaul were now considered necessary. In this broader context, therefore, TEC’s claim that the regulatory arrangements encourage excessive investment in transmission network is unfounded.

Furthermore, SP AusNet strongly disagrees that it would be appropriate to give priority to non-network solutions. SP AusNet agrees with ETNOF that such an approach would be contrary to the National Electricity Objective, which is focused on providing the most efficient outcome for customers in terms of price and reliability. Within this context, it is inappropriate to favour one type of solution compared to another, and the Rules presently reflect an unbiased approach to considering network and non-network solutions.

¹ Transmission Connection Planning Report 2007, produced jointly by the Victorian Electricity Distribution Businesses, page 20.

Whilst SP AusNet strongly disagrees with the principal elements of TEC's Rule change proposal, TEC does raise a number of issues that are worthy of further consideration. In particular, TEC has identified some important matters in relation to

- the possible introduction of a demand management incentive mechanism; and
- the need to clarify the arrangements for TNSPs to recover non-network costs.

In relation to the possible introduction of a demand management incentive mechanism, SP AusNet has a strong preference for financial incentives targeted at delivering efficient outcomes compared to administered rules. Therefore, the Commission may conclude that rather than requiring TNSPs to consider network and non-network solutions on an equal basis (as presently required by the Rules) it may be more appropriate to provide an incentive mechanism to encourage non-network solutions. The design of such an incentive mechanism would need to be carefully considered, and the Commission would need to be convinced that such an approach would be consistent with the National Electricity Objective. SP AusNet notes that provision for a demand management incentive scheme has been included in the recently finalised electricity distribution Rules.

In relation to the recovery of non-network costs, SP AusNet believes that there may be scope to improve the clarity of the existing Chapter 6A Rules. Whilst SP AusNet believes that the Chapter 6A Rules do provide for the recovery of efficient non-network costs, the provisions relating to this recovery are complex and open to different interpretations. The Commission may conclude that TEC is correct in that some incremental improvements to these provisions could be achieved.

SP AusNet would therefore support further work in relation to the development of a DM incentive scheme and measures to improve the clarity of the arrangements for TNSPs to recover non-network costs. We look forward to further opportunities to engage with the Commission in the development of any proposed Rule changes in relation to these issues, and we would be pleased to respond to any queries you may have on our submission.

Yours Sincerely



Charles Popple

GENERAL MANAGER REGULATORY AND BUSINESS STRATEGY

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