



2 April 2008

Australian Energy Market Commission
PO BOX A2449
Sydney South
NSW 1235

cc: submissions@aemc.gov.au

Review of the role of demand side participation in the National Electricity Market – Stage One

The Energy Supply Association of Australia (esaa) welcomes the opportunity to comment on Stage One of the Australian Energy Market Commission's (AEMC) Review of the role of Demand Side Participation (DSP) in the National Electricity Market (NEM).

esaa is the peak industry body for the stationary energy sector in Australia and represents the policy positions of the Chief Executives of over 40 electricity and downstream natural gas businesses. These businesses own and operate some \$110 billion in assets, employ over 40,000 people and contribute \$14.5 billion dollars directly to the nation's Gross Domestic Product.

esaa supports the role DSP can play in achieving the efficient supply of electricity. esaa defines demand management as actions to alter the level or pattern of the consumption of energy, or use of the energy network, in response to efficient prices or other incentives that efficiently minimise the cost of energy services. esaa's policy position therefore is that DSP should be facilitated via open and competitive markets that allow for efficient cost-reflective pricing and through effective incentive-based economic regulation of networks that appropriately rewards networks owners for innovation and investment in DSP.

esaa understands that the purpose of the Stage One review is to consider DSP in the context of the AEMC's current work program. AEMC has engaged NERA Economic Consulting to develop recommendations that can be assessed against current Rule change proposals and the scope and objectives of various AEMC reviews, specifically those related to national transmission planning, congestion management and the NEM reliability settings. Assessment of NERA's recommendations by the AEMC will be guided by the National Electricity Objective and by whether they are likely to deliver more efficient outcomes.

The conceptual framework developed by NERA for the role of DSP in the NEM advocates the primacy of pricing in promoting efficient electricity usage and optimal demand side participation. NERA finds that provided customers face the marginal network and generation costs of providing electricity services at their location they will choose to manage their demand appropriately by directly reducing load or investing in energy efficiency measures. Fundamental to NERA's framework is that intervention is only required where price signals are inhibited. Where this is not feasible unbiased incentives should be developed for Network Service Providers (NSPs) to consider DSP.

esaa fully supports this approach to facilitating DSP and informing subsequent stages of the AEMC review and endorses the draft recommendations which focus largely on addressing existing information asymmetries around the costs and benefits of DSP solutions to enable NSPs and NEMMCO to more accurately value such options within their internal planning processes.

While the scope of Stage One is constrained by the terms of reference provided by the AEMC, the NERA report highlights several key issues that esaa would expect to be examined in further detail throughout the later stages of the DSP review. In particular, NERA states that the principal impediment to DSP in network planning and investment 'arises because charges for the provision network services are usually independent of a customers location within the network, whilst the marginal costs associated with providing network services to a location vary'¹. As a result, by virtue of not being exposed to the marginal price signal, customers face little incentive to adjust demand resulting in decreased efficiency and sub-optimal demand side participation.

In addition, there are a range of other impediments that NERA identifies that are also considered beyond scope but which warrant further consideration. esaa believes that these are valid issues that deserve detailed consideration and encourages the AEMC to ensure that future processes deliberately and explicitly consider the issues including:

- Impediments to increased DSP among large end-use customers related to access to tariff products, lack of awareness of cost savings and high transaction costs associated with directly managing wholesale prices;
- Connection arrangements for distributed generation;
- Incentives for retailers to offer time-of-use products and manage wholesale price risk via demand-side options;
- Potential for biases against DSP within the incentives created via transmission network service costs and price regulation;

¹ NERA DSP Stage One Report, pg 14. NERA notes that locational cost signals are being enhanced in transmission planning through the introduction of locational transmission use of system service charges.

- Potential for biases against NSPs investing in non-network solutions resulting from the incentives created within network investment framework, such as obligations to satisfy reliability standards.

As a final point, esaa notes the timeframes for some of the relevant AEMC reviews are currently not aligned with Stage One of the DSP review and therefore the scope for any final Stage One recommendations to be considered by these reviews may be restricted. In particular, the AEMC has indicated consideration of Stage One findings for the Congestion Management Review (CMR) will be limited to NERA's draft recommendations and should NERA's final recommendations alter significantly from the draft report, the consideration of material changes as part of the National Transmission Planner (NTP) review may be limited.

Notwithstanding the limited scope of Stage One and the current timing mismatch with the CMR and NTP reviews, esaa endorses the NERA report recommendations and fully supports the proposed emphasis on pricing as the most efficient means to facilitate DSP in the National Electricity Market. esaa encourages the AEMC to explicitly address the various impediments to DSP highlighted in the NERA report during subsequent stages of the review process and looks forward to providing further commentary on these issues in due course.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Brad Page', with a stylized flourish at the end.

Brad Page
Chief Executive Officer