19 March 2015

energex
positive energy

Mr John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Dear Mr Pierce

Consultation Paper: National Electricity Amendment (Demand Management Incentive Scheme) Rule 2015 (ERC0177)

Energex Limited (Energex) appreciates the opportunity to provide a submission to the Australian Energy Market Commission (AEMC) on the consultation paper relating to reform of demand management incentives (consultation paper).

The consultation paper seeks stakeholder comment on rule change requests made by the COAG Energy Council and the Total Environment Centre (TEC) based on recommendations made by the AEMC in the Power of Choice review, the aims of which are to strengthen incentives for distribution businesses to pursue demand management projects as an efficient alternative to network capital investment.

Energex has a number of corporate strategies in place to manage its network to deliver balanced outcomes that meet the needs of electricity consumers, including management of peak demand on the network. Demand management has been a critical component in the efficient design, construction and operation of the Energex network for decades and has helped contribute to record low levels of forecast growth-related augmentation for the forthcoming regulatory control period.

While growth in overall demand is decreasing in response to a range of factors, such as reduced consumption and mild weather, long-term forecasts indicate future growth in localised peak demand which will lead to a renewed need for additional investment in network capacity. When effectively implemented as a first response solution, demand management will continue to reduce localised forward growth in demand resulting in lower future infrastructure-related electricity costs for consumers, more efficient management of technical issues on the network as well as benefits to the wider electricity supply chain. Energex is therefore supportive of reforms intended to strengthen incentives for distribution businesses to pursue efficient demand management and embedded generation connections.

Energex's responses to the issues raised in the consultation paper are provided in **Attachment A**. As a member of the Energy Networks Association (ENA), Energex has also contributed to and is supportive of the views contained in the ENA's submission.

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Energex looks forward to engaging in any further consultation on the development of the proposed DMEGCIS. Should you have any queries regarding this submission, please contact Rachel Leaver, Network Regulation Manager, on (07) 3664 4115.

Yours sincerely

Neil G. Andersen

Neil Andersen
Group Manager Regulation and Pricing

Issue 1: Issues this rule change is seeking to address

Despite changes in market conditions and the regulatory framework since completion of the Power of Choice review, Energex agrees with the rule change proponents' view that the current framework may not be providing sufficient incentives for distribution businesses to pursue demand management projects as an efficient alternative to network investment. Energex considers that this may be due to insufficient certainty for distribution businesses with respect to the application of the current scheme. Incentive schemes for demand management should provide for long-term certainty of investment in demand management activities and effective, widespread demand management requires the establishment of markets that take significant time to develop and mature.

The Australian Energy Regulator's (AER's) recent draft determination for Ausgrid is an example of how mixed messages from regulatory bodies on the importance and application of demand management can lead to uncertainty. The AER has discounted the long-term benefits of Ausgrid's proposed demand management initiatives on the basis that they would be marginal once more cost-reflective tariffs are in place[1]. Energex considers that there needs to be financial incentives for distribution businesses to pursue broad-based demand management options that take into consideration the value of demand reductions to the wider energy supply chain and assist customers in responding to price signals to reduce peak demand. Tariffs alone are insufficient to efficiently manage peak demand as they are a particularly blunt instrument which does not target regions of network constraint or days where demand is high. Tariffs and demand management programs are complementary and best results are achieved when they are used in tandem.

Issue 2: Proposed DMEGCIS

The COAG Energy Council and TEC have both raised legitimate factors that need to be considered by the AER in the application of the proposed Demand Management and Embedded Generator Connection Incentive Scheme (DMEGCIS). Energex therefore supports the inclusion of a high level objective and principles in the National Electricity Rules (the Rules), to be supplemented by more detail in the proposed guidelines to be developed by the AER (the guidelines).

In Energex's view, however, some of the detail provided in the proponents' rule change requests may be more suitable for inclusion in the guidelines rather than in the Rules. Furthermore, care should be taken to ensure there is an appropriate balance between prescription and flexibility in both the Rules and the guidelines so as not to create barriers for distribution businesses in pursuing demand management options. Consequently, Energex is of the view that the merit of each of the objectives and principles raised in the two rule change requests, and whether they should be included in the Rules or the guidelines, should be considered as part of further consultation.

With respect to the connection of embedded generators, while there are clearly compliance obligations in the Rules to further enhance the ability for embedded generators to connect to the network, Energex considers there may also be some benefit in providing additional financial incentives for innovation.

[1] AER Draft Decision, Ausgrid Distribution Determination 2014-19, Attachment 7: Operating Expenditure, 7-247.

Issue 3: Demand management innovation allowance

Energex supports codifying the requirements of the innovation allowance in the Rules to provide certainty to distribution businesses that the allowance will continue to be applied consistently. Greater certainty and a more effective incentive regime should increase the likelihood of participation in the scheme by distribution businesses.

Energex agrees with the ENA's view that the size and application of the innovation allowance should be determined by the AER and that the innovation allowance should be a time-limited measure. In determining appropriate timeframes, Energex considers that the AER should be required to take into consideration the maturity of the market and provide sufficient notice of when the allowance will be phased out to ensure visibility for future planning.

Issue 4: Demand management incentive scheme

Energex supports the proposal that distribution businesses should be able to receive a payment based on a proportion of the market benefits produced by a demand management project. Additionally, due to the long-term nature of the benefits provided by demand management projects, the framework should require the AER to allow for benefits delivered outside of the regulatory control period in which the project is delivered.

Energex supports the proposal to amend the Rules to require the inclusion of a payment for any foregone revenue resulting from implementing a demand management project approved under the innovation allowance. The operation of the incentive scheme should not pre-empt that a particular form of control will always apply.

In Energex's view, the proposed DMEGCIS should include both tariff-based and non-tariff based options to provide a suite of tools with which distribution businesses are able to manage demand. Broad-based tariff options can be used to lower customer demand and defer capital expenditure, while non-tariff demand management can be both broad-based and targeted to specific network constraints (such as specific geographical areas, customers or days).