

16 May 2011

Mr John Pierce  
Chairman  
Australian Energy Markets Commission  
PO Box A2449  
Sydney South NSW 1235  
Online lodgement via: [www.aemc.gov.au](http://www.aemc.gov.au)

Dear Mr Pierce

## **SUBMISSION ON AEMC STRATEGIC PRIORITIES FOR ENERGY MARKET DEVELOPMENT – DISCUSSION PAPER**

Endeavour Energy appreciates the opportunity to provide the Australian Energy Markets Commission (the “Commission”) with comments on the *Strategic Priorities for Energy Market Development – Discussion paper*. The discussion paper provides an important ‘check point’ of both the journey of the market to date as well as a guide to its future development.

Endeavour Energy has recently become a distribution-only business, and as a consequence this submission will focus on those matters relevant to the economic regulation of network service providers and the role that distribution networks play in achieving the optimal whole of market outcomes to consumers and investors.

### **Priority Area 1 – the investment environment**

While Endeavour Energy considers that main focus of the AEMC’s first priority area – the investment environment - to be on the generation sector, several identified drivers resonate throughout the energy market supply chain. In particular, peak demand growth has a significant impact for distribution networks, especially those that service the higher growth areas throughout Australia. The changing nature of peak demand growth over the past decade has been identified as one of the key drivers of network investment in NSW, along with the significant renewal programs currently being undertaken.

One of the emerging challenges for distribution networks is the impact and facilitation of generation from low carbon sources. As electricity networks were traditionally designed for the one way flow of electricity from large coal-fired generators to load supply areas, the proliferation of embedded generation and micro generation from sources such as solar panels may have implications for the design and safety (and its associated investment) in catering for the bi-directional flows of electricity.

### **Priority Area 2 – demand side participation**

The most significant issue to be addressed by the second priority area – demand side participation – is that of rising prices. There has been much debate on recent price increases and speculation over



future price changes, and there is little doubt that customers are more aware of their energy bills today than in previous years.

Demand side participation is in its infancy in Australia and increased demand side participation has the potential to ease the burden of rising prices and to empower customers to better manage their bills. It is apparent that the rules surrounding demand side participation have not been sufficient to facilitate growth in this area and need to be reviewed.

Endeavour Energy supports the Commission's review of the National Electricity Rules to ensure any legislative or regulatory barriers to demand side participation across the supply chain are removed. In this regard it will be important for the regulatory framework to support and encourage appropriate investments in smart grid and smart metering technologies to assist in enabling heightened demand side participation where the benefits of doing so outweigh the costs.

### **Priority Area 3 – the transmission framework**

Several elements of the Commission's work program for this third priority area are currently underway and Endeavour Energy looks forward to continued participation in these processes moving forward. Endeavour Energy notes that priority three appropriately focuses on the interactions between transmission and generation and the resultant market implications. However, Endeavour Energy is conscious that much of the current work program being undertaken in this area is equally applicable to distribution networks.

Our main focus for the Strategic Priorities Discussion Paper is to ensure appropriate consideration of aspects of network regulation (for both transmission and distribution) as may apply to Endeavour Energy in its capacity as an electricity distribution business, including:

1. *The expected AER review of its experiences with the current regulatory package and any resultant Rule change proposals to the AEMC`*

The AER's review and subsequent recommendations are expected to occur over the next few months. This review will be an important summary of lessons learnt and to understand the AER's perspective on those aspects of the regulatory regime that are working well and those areas where there is room for improvement. Specifically, the AER's insights on the current level of information, interactions with industry participants and consumer representatives and the clarity of the National Electricity Law and Rules in practice will be of benefit to the market. The appropriate level of regulatory discretion available to the AER in enforcing the Rules in order to achieve the National Energy Objective will be a key area of focus for any rule change proposal.

Endeavour Energy considers that any review by the AER would be best dealt with through the AEMC's rule change process, rather than as a component of the Strategic Priority review.

2. *The development of a national information reporting regime by the AER.*

Endeavour Energy is aware that the AER is commencing the development of a national information reporting regime. The development of a national set of reporting requirements will pose several challenges for the AER, as it will need to devise a means to harmonise different reporting regimes in each jurisdiction. More importantly, the AER will need to demonstrate to customers that they have achieved an appropriate balance between information provision and consistency against the potentially considerable costs associated



with system changes, annual reporting processes and independent “positive assurance” reviews.

3. *The AEMC review into Total Factor Productivity (TFP)*

Endeavour Energy has been an active participant in the AEMC’s review of TFP. While we believe that the review process has been informative, we do not believe that TFP is well suited as a primary form of regulation for setting regulated revenues or prices for an individual electricity network business.

Benchmarking, including the use of TFP, can offer valuable insights into the efficiency of a business’s specific operations, and as such its use as a management tool to assess the performance of individual activities is appropriate. Extending the use of TFP to the setting of regulatory revenues is not supported at this time – we believe it more appropriate to contemplate such a move only after a comprehensive review of the current framework and all viable alternatives has been undertaken (such as occurred in the UK with the OFGEM “RPI-X@20” review).

4. *The potential review into the magnitude and regularity of matters referred to the Australian Competition Tribunal (ACT).*

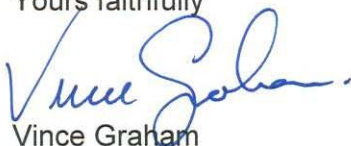
Endeavour Energy has some reservations as to the approach and criteria that would be applied to such a review. We note that there have been several matters referred to the ACT for review on the merits of the AER’s decisions, and in the majority of cases the ACT has found in favour of the businesses and that the AER had erred in its decision making.

There has been considerable public attention on the need to review the regulatory framework in light of rising electricity prices and that the availability of merits review has contributed to these increases. Endeavour Energy considers that, to facilitate long term efficient investment in infrastructure, any changes to the current regulatory framework to expressly include short term pricing impacts to customers in regulatory decisions should be clearly articulated in the Rules as to their application, rather than allowing unfettered regulatory discretion.

It should also not be unexpected that the move to a national regulatory framework would entail a review of regulatory decisions in certain instances as industry participants (including customers) seek to establish how regulatory discretion is to be applied. While it is likely that the number of merits reviews will diminish over time as the application of the regulatory framework becomes more clearly defined, Endeavour Energy submits that it would be a retrograde step in achieving a best practice regulatory framework if appropriate checks and balances on the application of regulatory discretion are removed.

If you would like to discuss this submission further, please contact our Manager Network Regulation, Mr. Michael Martinson on 02 9853 4375.

Yours faithfully



Vince Graham

**Chief Executive Officer**