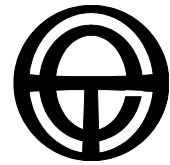


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Supplementary Working Paper

Total Environment Centre (TEC) welcomes the opportunity to continue the dialogue on the shape of the future Rules for distribution and retail. In this submission, we will only be addressing the position on the National Electricity Law Objective in the "Supplementary Paper", which is that it is sufficient for the purpose. We understand the impetus towards establishing a single objective – such as the need to replace prior, disparate objectives – however we consider the current objective deficient and that the establishment of two extra objectives would simplify certain problems rather than creating contradictions.

Our basic premise is that the two proposed objectives (an environmental and a social objective) are essential in the long-term interests of consumers to recognise that consumer protections are critical to reflect the essential service characteristic of electricity and the particular vulnerabilities of particular classes of consumers (since the current Objective does not distinguish). Further, there needs to be an explicit acknowledgement of the environmental damage that the supply and use of energy can inflict and hence undermine consumer interests, in particular greenhouse gas emissions which are now recognised to be a major contributor to climate change.

Although there is an assumption that these environmental and social concerns can be addressed outside the NEM by government policies and programs, in practice there are no overarching policies or regulations that deal directly with this range of issues. Approaches are piecemeal and vary widely across the jurisdictions – a national-level determination would lead to greater consistency and continuity. This would be to the advantage not only of end users but also market participants.

Environmental objective

The RPWG has recommended that a change to the objective is not required on the basis that, "this will be better addressed by more specific direction targeted at the particular regulatory functions concerned rather than at the level of the general objective." (p 2) However, they also state that, "By their nature, provisions dealing with enforcement and objectives are appropriate for inclusion in the Law." (p 4)

TEC contends that the Objective of the NEL is inadequate and the changes required for regulation of the NEM permeate throughout the National Electricity Rules (the Rules), rather than just referring to specific provisions. Rather, a change in emphasis is required. For instance, TEC has been advocating in many forums for the consideration of demand management¹ (DM) as a primary factor in decision making about the National Electricity Market (the NEM), in particular for incorporation of DM principles within the Rules. We consider DM to be such an important issue that we are of the opinion that specific considerations need to be developed to give direction to the Rules. Climate change due to human action is such a pressing issue that it needs to be addressed on all fronts, rapidly, particularly in terms of the reduction of greenhouse gas emissions.

Neglect of demand management is a pervasive problem throughout the Rules, despite professed intentions that demand side options should be given "due and reasonable consideration". The Rules state, for instance:

6.2.3 Principles for regulation of transmission aggregate revenue (d) "The regulatory regime to be administered by the AER ... must also have regard to the need to: (2) create an environment in which generation, energy storage, demand side options and network augmentation options are given due and reasonable consideration;"

However, there is no tangible support or incentive provided within the Rules for demand side options to be properly implemented. Lack of incentive mechanisms for the implementation of non-network solutions is resulting in inefficient, peak-driven transmission infrastructure investments. The NEM is inappropriately focused on the supply of electricity at the expense of a focus on the provision of energy services, including demand side or other non-network approaches. Little has changed in that regard since the Parer report² noted:

A key feature of competitive markets is the active participation of both the supply and demand sides. Without this, competition is blunted and the potential for the exercise of market power is enhanced. ... Many submissions to the Review contended that demand side involvement in the NEM is under-developed.

Any new specific content of the Rules will be insufficient to completely fulfil the opportunities afforded by a vigorous promotion of DM and embedded generation across the NEM unless there is also a statement of intent in an overarching Objective. Rather than there being specific barriers or problems with single Rules regarding DM and other non-network solutions, it is an oversight within the whole set of Rules that

¹ DM in this proposal can be read to include 'demand response', 'demand side management', 'demand side response', 'energy efficiency' and 'non-network solutions'. In general, DM can include both the management of peak loads and energy efficiency as a way of meeting capacity requirements most cost effectively. It includes a diverse array of activities that meet energy needs, including cogeneration, standby generation, fuel switching, interruptible customer contracts, and other load shifting mechanisms.

² Commonwealth of Australia, *Towards a Truly National and Efficient Energy Market*, 2002, p 173

needs to be addressed for the NEM Objective to be fully met. This is a market design deficiency that should be rectified. TEC believes that the problems resulting from this poor design can be resolved by a change to the Objective, that is, by the addition of extra Objectives.

It has been proposed in many options papers about the reform process that "environmental issues" be left to the jurisdictions. Mechanisms have been proposed for dealing with these issues, the primary one being a so-called "Jurisdictional Direction". Gilbert+Tobin created the term, and Clayton Utz is currently investigating the approach for the MCE's Retail Policy Working Group. Demand management is often sidelined as an environmental matter, therefore not something to be actively pursued within the NEM. This is a fallacy, since DM can make contributions in many ways – on top of bringing environmental benefits – to a more efficient and reliable electricity system. The main problem is that there has been insufficient uptake because of the weight of the status quo, the small number of solid examples and consequently the network providers' aversion to undertaking a potentially risky solution.

On the subject of efficiency, raised in the Supplementary Paper in relation to SCO's statements about changes to the NGL, there are many sides to efficiency. Economic efficiency is central to the NEM and to achieve this there must be equal emphasis on demand and supply. The neglect of DM again exemplifies this contradiction within the NEM.

It is obviously more in the interests of network and retail businesses to promote the consumption of more electricity and thus increase their revenue than to foster reduced demand in any form. In theory there is consumer choice in the market, but this choice cannot be exercised in relation to transmission network businesses.

Demand side opportunities include load shifting, load curtailment and fuel switching and these can represent a low cost alternative to generation and transmission investments. DM provides the potential for networks to operate more efficiently by avoiding unnecessary or premature network augmentations, and thereby create savings for consumers. Consequently the use of DM techniques can lead to better cost-reflective pricing and can have a downward pressure on prices (productive efficiency), which can also have long run effects on pricing (dynamic efficiency). Reliability benefits also have an effect on allocative efficiency.

DM exemplifies the benefits that would be more easily realised if there were an Environmental Objective established within the National Electricity Law and hence the Rules.

The Environmental Objective proposed in TEC's paper, "How should Environmental and Social Policies be Catered for as the Regulatory Framework for Electricity becomes increasingly National", is:

"The Market Environmental Objective is to contribute to achieving ecologically sustainable development and is to have regard to the effect on the environment of the generation, transmission, distribution, supply and use of electricity and related activities including achieving a permanent reduction in the total global emissions of greenhouse gases."

Social objective

Section 4.3 of the Supplementary Paper contains a discussion of consumer interests, and has been separated from the discussion on Objectives. In fact, if there were a social objective then it would also address some of the concerns raised in this section, such as the emphasis on economic efficiency noted in the Supplementary Paper. The paper states that for those who see the objective as deficient: "On that view, the existing objective does not give adequate scope for the AEMC and AER to give effect to equity issues and shorter term consumer welfare considerations."

As with an environmental objective, the conclusion in the paper was that, "this will be better addressed by more specific direction targeted at the particular regulatory function rather than at the level of the general objective." (p. 18) However, the same arguments apply here as for the environmental objective, that is, that neglect of these social concerns is pervasive through the Rules – and hence any directions to regulators – rather than relating to any specific provisions. There are no doubt specific Rules that could be amended, but it is nonetheless more a matter of emphasis and direction than a fault of specific details – therefore a high-level change is necessary.

The Social Objective proposed in TEC's paper is:

"The Market Social Objective is to promote the long term interests of consumers with respect to the supply of electricity as an essential service including addressing the particular vulnerabilities that particular classes of consumers may have such as customers who are: disabled or chronically sick; of pensionable age; of low income; and/or residing in rural areas."

Thank you for your attention.

Yours faithfully,



Jeff Angel
Executive Director