6 March 2009

Attention: Mr Chris Pattas
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Network Regulation South
Australian Energy Regulator
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By email to: aerinquiry@aer.gov.au

COMMENTS ON THE
PROPOSED DEMAND MANAGEMENT INCENTIVE SCHEME
Citipower, Powercor, Jemena, SP AusNet and United Energy
Regulatory Control Period commencing January 2011

Energy Response is pleased to have the opportunity to provide comments on this Proposal. Overall, we are very concerned that this is proposing a use of consumers' money to undertake R&D which would normally be funded by the owners of the business and be subject to special tax treatment.

However we also believe that it is not incentive that the Distribution Businesses require at this stage, rather it is the removal of a number of remaining disincentives. These are described below.

Our premise is that there is already a strong commercial incentive for any distribution business to work out how to improve their economic efficiency and hence profits. However, we would be supportive of incentives that come from the delivery of the use of non-networks solutions where appropriate so they can "learn by doing" and the consumers who participate will receive the benefits immediately.

The question is why are the DNSPs not doing this already? We understand from discussions with a range of DNSPs across the NEM that it is a number of disincentives that are minimizing the amount of DSR/DSM used to improve their economic efficiency.

Also, there does not appear to be anything in the Proposal to stop DNSPs spending the money on ineffectual R&D. What benefits have come from the $600,000 per DNSP from the current period? The assessment criteria are given in clause 3.1.3 of the main report. There is nothing about effectiveness or value for money – it appears to be a case of "is this a demand management or an R&D scheme"? If the proposed incentive is to proceed we strongly recommend:

- Adding an overarching criterion requiring demand management projects to demonstrate value for money, and
- (since it is the consumers' money) making any IP derived from the process publically available free of charge, and

- Removing criterion 3, as there's very little actual R&D to be done.

The Proposal does not address the largest disincentives that the DNSPs have raised with Energy Response. Addressing these will create much greater benefits for the use of DSR/DSM than this Proposal as it is. These disincentives are:

1. The first disincentive is that the DNSP's need regulatory certainty that a DSM/DSR project, eg, a non-network solution to defer capital expenditure, which commences in one Regulatory Period and continues to provide benefits into the next period will be guaranteed automatically under the first regulatory decision. Surely this can be done to ensure that once started a non-network project or other DSM/DSR project will be automatically approved in the next period without any further reference. This automatic approval in the next regulatory period already occurs for capital works once a project is commenced. This problem occurs both with projects which are planned during one control period but whose "delivery period" is in the next, and in projects whose delivery period spans two control periods.

2. The second disincentive relates to ensuring that non-network solutions receive equal treatment and planning consideration. It is essential to ensure that DSM/DSR (which is relatively new) and other alternatives such as distributed generation are not ignored or made too difficult in favour of the traditional build option. This will make the new requirements for consideration of non-network solutions introduced by the AER much more effective. This needs to be made uniform across Australia and the outcomes open to audit by the AER to ensure that the comparison of the options does result in the best outcome. The issue of deferral of capex by greater expenditure of opex needs to be including fairly in the process.

3. The third disincentive relates to foregone revenue. If the AER considers forgone revenue to be such a significant potential disincentive for DNSPs to conduct demand management projects that it would be worthwhile setting up the complex arrangements described in Part B, then it doesn't make sense to restrict such recovery only to foregone revenue due to demand management schemes funded through the DMIA. It should apply to all non-tariff based demand management schemes started on the DNSP's initiative. Otherwise, this has the effect of making the funds available under the DMIA into an *upper* bound on the amount that a DNSP will spend on demand management.

Once these disincentives have been removed the DNSPs will be able to make the best choices for themselves and these should also then provide the best outcomes for the consumers.

Yours faithfully

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