INFORMATION

EBSS and Demand Management Expenditure by TNSPs

Draft Determination 29 September 2011

The draft rule addresses a potential financial disincentive problem under the Efficiency Benefit Sharing Scheme (EBSS) for Transmission Network Service Providers (TNSPs) to pursue demand management expenditure as an efficient substitute for network investment solutions. The draft rule strengthens the scope and certainty for TNSPs to pursue demand management options and find an efficient balance between the need for additional network investment and the value of flexible demand.

The Commission has decided to make a draft rule in response to the request from the Ministerial Council on Energy (MCE) regarding the exclusion of non-network alternative expenditure from operating expenditure that is subject to the EBSS.

The draft rule proposes to require the Australian Energy Regulator (AER), in designing and implementing the EBSS, to consider the possible effects of the scheme on a TNSP's incentive for the implementation of non-network alternatives. The draft rule makes the EBSS arrangements for TNSPs on non-network alternative expenditure consistent with those for Distribution Network Service Providers.

Call for submissions

Submissions on the draft rule determination should be received by10 November 2011.

Proposal in context

In November 2009, the AEMC provided its stage 2 final report to the MCE identifying certain aspects of the existing National Electricity Rules that could be improved to enhance demand-side participation (DSP) in the national electricity market. The stage 2 DSP review raised the issue of the EBSS for TNSPs as an area needing further consideration.

The purpose of an EBSS is to encourage cost efficiency by providing an incentive mechanism through which TNSPs can earn additional revenue or be penalised depending on whether the business beats or exceeds targets for its operating expenditure in each year of the regulatory control period. Since expenditure on DSP solutions are largely in the form of on-going operating expenditure, the AEMC's DSP review found that the EBSS may potentially create disincentives for a TNSP to consider efficient non-network alternatives as it may lead to reduced financial rewards or even penalties.

The National Electricity Rules require the AER to establish and apply an EBSS for TNSPs. However, the rule establishing the EBSS framework currently does not require the AER to consider how the scheme might impact on a TNSP's incentives to pursue efficient DSP solutions.

In response to the stage 2 DSP review findings, the MCE submitted a rule change request in November 2010 to exclude non-network alternative expenditure from the EBSS to address the potential disincentive effect. The MCE proposed a rule to expand the scope of the EBSS rule to require the AER to consider the scheme's effect on a TNSP's incentive to incur non-network alternative expenditure.

On 23 June 2011, the Commission published a notice under section 95 of the National Electricity Law (NEL) advising of its intention to commence the rule making process and the first round of consultation in respect of the rule change request. Submissions closed on 21 July 2011.

The Commission received four submissions on the rule change request as part of the first round of consultation. All submissions were in favour of the MCE's proposed rule.

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The draft rule strengthens the scope and certainty for Transmission Network Service Providers (TNSPs) to pursue demand management options and find an efficient balance between the need for additional network investment and the value of flexible demand.

Draft Rule Determination

The AEMC's draft rule determination notes that the AER has already moved to recognise the impact of the EBSS on a TNSPs' incentives for pursuing DSP solutions by excluding non-network alternative expenditure from the EBSS. While the AER's more recent decisions on the EBSS effectively neutralises the materiality of the problem identified in the rule change request, the current EBSS framework for TNSPs does not ensure that the AER will consistently consider the incentives for non-network alternative expenditures when it applies the EBSS to TNSPs revenue determinations.

The current lack of certainty and consistency in how a TNSP's non-network alternative expenditure may impact on its EBSS reward/penalties for the next regulatory period makes it unlikely that a TNSP will take a risk by substituting more economically efficient demand- side solutions with network solutions.

The draft rule clarifies the issue by making it an explicit requirement for the AER, in designing and implementing the EBSS, to consider the scheme's efficiency reward/penalty effects on incentives for a TNSP to undertake non-network alternative expenditure on a consistent basis. This should provide TNSPs more confidence to pursue demand management options and find an efficient balance between the need for additional network investment and the value of flexible demand.

The draft rule does not define or categorise non-network alternative expenditures for the purposes of the EBSS. The Commission believes that objective of the draft rule is more likely to be achieved by allowing the AER discretion in deciding the types of non-network alternative expenditure it will exclude from the EBSS on a case by case basis. In this regard, the draft rule provision is consistent with the treatment of non-network alternative expenditure in the EBSS framework for Distribution Network Service Providers.

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