Department of State Growth

Tasmanian Energy Strategy

Issues paper

Submission - response

September 2014

Acknowledgements & Disclaimers

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Executive Summary

This submission responds to the Department of State Growth's *Energy Strategy Issues Paper* (the Issues Paper) released on 12th August 2014.

The TSBC welcomes the development of the (Tasmanian) Energy Strategy which is long overdue and will provide the opportunity for a coordinated, focussed approach to managing the energy challenges which confront Tasmania. The TSBC believes that to be fully effective, the Energy Strategy must be non-partisan with broad political support as well as the endorsement of key stakeholders including business representative bodies.

The Independent Review of the Tasmanian Electricity Supply Industry, commissioned by the (previous) government and conducted by an Independent Expert Panel[1], provides excellent guidance that the TSBC strongly recommends the current government follows, where recommended changes have not yet been implemented, as part of the Energy Strategy.

The TSBC notes that successive Tasmanian governments have failed to adequately address two major issues, being the introduction of a wholesale electricity market, and the privatization of electricity assets, both of which are impediments to achieving the lowest cost electricity prices achievable in the State.

The TSBC strongly recommends that the Government adopt the recommendations of the Expert Panel relating to establishment of a competitive wholesale electricity market. That step is fundamental to the successful introduction of retail competition.

The TSBC contends that there has been no informed debate on the merits or otherwise of the privatization of electricity assets. The number and scale of changes in the local electricity market since energy reforms began in the 1990s, including Tasmania's entry to the National Electricity Market and the supply/demand situation, have fundamentally changed the environment in which the Tasmanian state owned electricity businesses operate, along with the risks and rewards of ownership and the very large financial consequences. The current oversupply of electricity and the associated financial implications provide stark evidence of those risks.

The TSBC sees five major principles fundamental to the energy strategy:

1. Energy is produced and delivered via the most cost effective means possible, noting that this must be over the long term, i.e. sustainable;

1 Independent Review of the Tasmanian Electricity Supply Industry, final report, March 2012

2. Energy consumption across all customer groups is as low as possible in order to meet customer requirements (thereby limiting the scale of investment in energy infrastructure and input costs);

3. The prices charged for energy to each customer group (or class) reflect the cost of production and delivery. (Implication – categorization of customer classes is appropriate, and there are no cross-subsidies);

4. Any variation of prices in order to achieve social equity outcomes is transparent and funding for any resulting subsidies is transparent and equitable;

5. All customers are empowered - with information about their energy use in a time frame (real time, monthly) which suits their needs; with the capacity to respond to the information as they choose; and with choices about how they use energy and who they purchase it from.

Those principles are in the main aligned with the suggested outcomes of the Energy Strategy, as proposed in the Issues Paper (p25).

The TSBC notes the establishment of the Energy Working Group and considers that giving the Working Group a meaningful role in the development and implementation of the Energy Strategy represents good governance.

This submission provides detailed responses to each of the 14 questions posed in the Issues Paper, as well as a summary of the TSBC's position on each question.

A theme throughout the TSBC's responses and positions is the need for effective competition and removal of regulation wherever possible throughout the electricity supply chain, noting that whilst the natural gas market is fully contestable, the small scale of the market means there is little competition in practice.

A second theme is that wherever regulatory intervention exists or is proposed, the demonstrable benefits of that intervention must outweigh the costs imposed on small business and domestic customers, including direct and indirect costs.

TSBC members expect that efficiency gains, recent significant network investments and enhanced planning processes, will see reliability of electricity supply improve, without extra cost. The TSBC notes the development at a national level of a regulatory framework to enable an economic assessment of the reliability/cost trade and proposes that the Energy Strategy should incorporate that development.

The TSBC suggests that existing electricity network (and retail) tariffs are not cost reflective and include inappropriate cross subsidies which penalise small business. Further, changing the structure of network tariffs to reflect the cost of meeting different levels of peak demand will, over time, deliver lower electricity prices to all customers and help eliminate existing cross subsidies.

Changes to network tariffs are part of a larger issue, being consumer engagement in managing their electricity consumption, and must be accompanied by changes in the way in which information about consumption and prices is provided to electricity customers.

We note the development at a national level of a series of actions to progress such changes and we propose that the Energy Strategy should incorporate that development.

The TSBC does not support Government intervention in the setting of wholesale or retail electricity prices for domestic and commercial customers in order to stimulate load growth, or to support the financial position of the state owned electricity businesses.

Competitive wholesale and retail markets are the TSBC's preferred options for price setting, which would over time deliver reduced electricity prices to small business and other electricity users.

In seeking to increase load growth and utilise assets which currently have surplus capacity, by attracting new customers, the TSBC suggests that Tasmania does have a range of competitive advantages such as relatively low cost land and accommodation, both industrial and domestic, which should be promoted by the Department of State Growth in its efforts to attract new business.

The rapidly rising cost of natural gas and its impact on the viability of small business using gas is of major concern to the TSBC, however the TSBC urges caution before the Government considers investigating options to intervene in what is a fully commercial, unregulated market, with willing participants.

Instead, the TSBC recommends that the Government, through its Council of Australian Governments and Standing Council on Energy and Resources roles, plays an active role in bringing on a policy discussion concerning a gas reservation policy.

The TSBC has proposed a broad outline of the contents of the Energy Strategy, which would include section one covering immediate challenges and actions and section two covering a description and evaluation of long term credible scenarios and actions associated with the most likely scenario.

The TSBC recommends that the findings and recommendations of the Expert Panel's Independent Review should form the basis of the immediate challenges and actions section of the Energy Strategy and that any development of renewable energy by the Government or by state owned electricity businesses should be guided by the Energy Strategy and be subject to business case evaluation.

The TSBC has sought advice on the future key drivers which will shape Tasmania's energy futures, section two in its proposed structure of the Energy Strategy. Each of the drivers examined will shape the scenarios which actually evolve, and each presents challenges and

opportunities, which will be the subject of government decision making. Those decisions will play a significant role in determining which scenario actually emerges in the future.

The TSBC believes that a critical component of the Energy Strategy is the development of a range of credible scenarios which may then be subject to detailed analysis of predicted economic and social outcomes to inform the Government's decisions.

The TSBC's recommends its proposed broad structure/contents for the Energy Strategy should be implemented by an appropriately resourced project team, guided by a comprehensive implementation plan.

The Government and key stakeholders will then be in a position to measure performance/success by:

- Assessing progress against the implementation plan; and
- Determining whether the Strategy's objectives have been achieved, by reference to measurable targets.

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1 Introduction

This submission responds to the Department of State Growth's *Energy Strategy Issues Paper* (the Issues Paper) released on 12th August 2014.

The TSBC welcomes the development of the (Tasmanian) Energy Strategy which is long overdue and will provide the opportunity for a coordinated, focussed approach to managing the energy challenges which confront Tasmania. It provides the opportunity to avoid past mistakes, including the failure of the process to sell Aurora's customer list and the process to acquire the Tamar Valley Power Station, both involving substantial initial and ongoing cost.

The TSBC suggests that the answers to most of the questions in the Department's Issues Paper, to which this submission responds, have been provided in many submissions and reports, either directly to this government or its predecessors, or via regulatory processes, and in publicly available reports produced by a range of qualified commentators.

In particular the Independent Review of the Tasmanian Electricity Supply Industry, commissioned by the (previous) government and conducted by an Independent Expert Panel[2], provides excellent guidance that the TSBC strongly recommends the current government follows, where proposed changes have not yet been implemented.

The TSBC notes that there appear to be a number of "elephants in the room" that successive Tasmanian governments have failed to adequately address. The two major issues are the introduction of a wholesale electricity market, and the privatization of electricity assets.

The benefits of the introduction of a wholesale electricity market were clearly explained by the Expert Panel, including a comprehensive analysis of options and the relative merits of each. The TSBC strongly recommends that the Government adopt the recommendations of the Expert Panel relating to establishment of a competitive wholesale electricity market.

The TSBC holds no firm view on the issue of privatization but contends that, since the 1998 state election, at which the then Liberal minority government headed by Tony Rundle proposed the sale of the state's transmission, distribution and retail assets but lost the election, there has been no informed debate on the merits or otherwise of privatization of electricity assets. The number and scale of changes in the electricity market, including the supply/demand situation, and Tasmania's entry to the National Electricity Market have

2 Independent Review of the Tasmanian Electricity Supply Industry, final report, March 2012

however fundamentally changed the environment in which the Tasmanian state owned electricity businesses operate, along with the risks and rewards of ownership.

The TSBC regards that situation as an abrogation of duty by successive governments, given the significance of the issues and the very large financial consequences associated with the range of choices.

The TSBC is of the view that if the choices and the consequences were properly analyzed (the Independent Review provides the foundation of such analysis) and presented to the Tasmanian public, and meaningful debate was promoted, then the current attitude of "no privatization" without explanation may change.

The TSBC looks forward to participating in that debate.

In preparing this submission the TSBC has drawn on its members' views and the broad information base available to it in providing its responses. Where there are common themes in the available information set we have sought to highlight those in our responses.

The TSBC suggests that the very long term investment in energy infrastructure should be matched by a long term Energy Strategy to guide that investment and endorses the proposed lifespan of the Energy Strategy of 20 years as a first step, noting that most government energy strategies have a lifespan of 30 or 40 years. The TSBC further suggests that such a strategy can only be effective if it is non-partisan and has broad political support, as well as the support of energy market participants and energy consumers and their representative bodies.

The TSBC notes that substantial, relevant inputs to the Energy Strategy, such as the former federal government's Energy White Paper, "Australia's Energy Transformation", 2012, and the Climate Smart Tasmania Report 2013, both the subject of lengthy developments including extensive public consultation, have become inaccessible to the public. The TSBC is of the view that the development of the Energy Strategy is too important for such significant and informative work to be excluded from consideration and suggests they form part of the Department's deliberations.

The Energy Strategy must be sufficiently well developed to enable changes such as economic climate, energy usage patterns and technology to be accommodated, but its value would be minimised if changes of government, rather than changes in external factors, resulted in major changes to the Strategy.

The TSBC sees five major principles fundamental to the energy strategy:

1. Energy is produced and delivered via the most cost effective means possible, noting that this must be over the long term, ie sustainable;

2. Energy consumption across all customer groups is as low as possible in order to meet customer requirements (thereby limiting the scale of investment in energy infrastructure and input costs);

3. The prices charged for energy to each customer group (or class) reflect the cost of production and delivery. (implication – categorization of customer classes is appropriate, and there are no cross-subsidies);

4. Any variation of prices in order to achieve social equity outcomes is transparent and funding for any resulting subsidies is transparent and equitable;

5. All customers are empowered - with information about their energy use in a time frame (real time, monthly) which suits their needs; with the capacity to respond to the information as they choose; and with choices about how they use energy and who they purchase it from.

Those principles are in the main aligned with the suggested outcomes of the Energy Strategy, as proposed in the Issues Paper (p25).

The Issues paper notes that its proposed outcomes, "are provided on the basis of assisting respondents to consider what outcomes they might like to see."(p3).

The TSBC's views on the proposed outcomes are discussed at section 2 in response to question 14.

The TSBC notes the establishment of the Energy Working Group and considers that giving the Working Group a meaningful role in the development and implementation of the Energy Strategy represents good governance.

1.1 Background to Tasmanian Small Business & the TSBC

There are more than 37,000 small businesses in Tasmania, 22,000 of which are "employers'. The enterprise of small business is estimated to provide Tasmania with more than 110,000 full and part time jobs. Numerically, small businesses make up 96% of all businesses in Tasmania. Estimates in previous industry surveys[3] indicate that around 70% of all employment in Australia is provided by enterprises with less than 20 employees.

Understanding the small business sector, its aspirations and needs is of vital importance to the enterprises themselves, as well as Government and regulators as decision-maker. The resources to address the future needs of the state can only come from the generation of new wealth and healthy, vibrant small businesses are critical to this.

The Tasmanian Small Business Council (TSBC) is an "association of [small business] associations", each of which represents their market grouped industry sector. The TSBC

3 Price Waterhouse Coopers

seeks to provide the representative voice of small business in Tasmania. The TSBC's role in facilitating meetings of and forums for these trade associations, whose members are predominately small businesses, is paramount to providing informed insights and advice to governments and regulators.

An obvious difficulty for owners of small and micro businesses is the absolute necessity to spend their time working "in the business", while those with larger numbers of employees take a more managerial role and begin to spend some of their time working "on the business".

Small business is therefore even more reliant on groups such as the TSBC to develop and put forward informed policy positions to Government and regulators that truly represent their interests.

1.2 TSBC's Interest in the Energy Strategy Issues Paper

A reliable and cost-competitive energy supply is vital to the success of small business in Tasmania. Electricity costs represent around 3 to 5 percent of input costs of the average small business, therefore keeping those costs as low as possible is important to the financial success of the sector.

Many small businesses are in direct competition with mainland or international businesses which have access to lower cost energy, or are able to take advantage of more competitive energy packages, and many face growing competition from on-line sellers. For those businesses, particularly those with relatively high energy consumption, energy price increases beyond CPI can seriously erode financial viability.

Access to a highly reliable (continuous) supply of electricity is of critical importance to a substantial portion of small business, such as those delivering seafood or dairy products into time critical markets, or those providing 24 hour internet services.

The TSBC has participated in the consultation process around Tasmania's energy market reforms to the maximum extent of its resources, in order to ensure that its members' views are heard and considered in any related policy decisions.

The TSBC has been disappointed with some aspects of the energy reform process to date and welcomes the opportunity to see the reform process confront what it sees as shortcomings which have yet to be addressed.

1.3 Outline of This Submission

In preparing this submission (response) we have considered a range of publicly available information, including, but not limited to:

- The AEMC's Power of Choice; Reliability Standards and Settings; and Energy Adequacy Assessment reviews;
- The Review of Tasmania's Electricity Supply Industry by the Tasmanian Government's appointed Electricity Supply Industry Expert Panel;
- The current federal government's Issues Paper for a New Energy White Paper;
- The Tasmanian Renewable Energy Industry Development Board advice to the Tasmanian Government on a Tasmanian Renewable Energy Strategy, August 2011;
- The Grattan Institute Fair Pricing for Power report; and
- TSBC's previous submissions pertaining to the questions posed in the Energy Strategy Issues Paper.

The TSBC's approach to the submission is, where possible, to draw on and reference that material, rather than seek to re-state positions which have already been presented, and where applicable to point out where there are consistent messages across a number of information sources.

The remainder of this submission is structured as follows:

Section 2 - We respond separately to each of the 14 questions in the Issues Paper, drawing on our members views on the questions and also relevant publicly available material. Many of the questions have been debated in the national forum, or as part of Tasmania's energy reforms to date, and the TSBC has previously provided input into some of those debates.

Section 3 - We include a summary of the TSBC's position on each of the 14 questions.

Questions posed by the Department of State Growth

Question 1

What enhancements could be made to regulatory frameworks to ensure the right incentives for businesses and consumers are in place?

TSBC response

The Energy Strategy Issues Paper (to which this submission responds) asserts, at page 4:

"… the Electricity Supply Industry Expert Panel, established by Parliament, conducted a thorough investigation and delivered a detailed report in 2012 on structural and market options. The response to that report resulted in a number of structural changes that have now mostly been put in place", and:

"The main change that has not been implemented is the sale of Aurora's customer list". (emphasis is TSBC's).

The TSBC contends that both those statements are open to question.

Reform of electricity markets around the world and in Australia has inevitably been preceded by the establishment of competitive wholesale electricity markets. Tasmania's electricity reforms to date have not resulted in the establishment of a competitive wholesale electricity market, despite overwhelming evidence suggesting that is a vital omission.

There is no new evidence or argument to add to previous considerations of an appropriate wholesale market structure for Tasmania, however the TSBC believes it is appropriate to remind decision makers of a very small sample of the evidence and argument previously provided to the Government.

The Electricity Supply Industry Expert Panel report's first recommendation was:

"1. wholesale market structural reform – The separation of Hydro Tasmania's physical generation operations from its financial trading functions and the transfer of these trading functions to three specialised, independent state owned trading entities (referred to as 'GenTraders');"[4]

4 An Independent Review of the Tasmanian Electricity Supply Industry, Final report volume 1, March 2012

It is the TSBC's view that the reasons outlined in the Expert Panel report for that recommendation are clear and compelling.

In its March 2013 submission responding to the Tasmanian Energy Reform, Market and Regulatory Framework Position Paper, the TSBC previously stated:

> "The TSBC recognises the critical role that the wholesale market plays in Tasmanian electricity reform. It does not, however, agree with the Government's view that the Tasmanian hydro-electric system necessarily needs to be run as if it were a natural monopoly. It therefore does not accept that regulation of the wholesale electricity market is the best approach to reform. Following its extensive (and expensive) investigation, the Independent Panel certainly did not think so, opting instead for a solution involving wholesale competition and dismissing the regulatory approach as inferior.
>
> The TSBC is concerned both about this divergence of views and that the Government's choice may constrain retail competition".[5]

That concern was translated into reality following the failure to secure a buyer for Aurora's retail base. The TSBC commented in its November 2013 submission to the Tasmanian Economic Regulator:

> "The absence of serious bidders for Aurora's retail base represents a very poor outcome for Tasmanian electricity consumers and calls into question the Government's reform strategy and the reasons behind it. It is even more disappointing given that the Expert Panel clearly warned about the flaws in regulating the wholesale market and the disincentives that this would create for new entrants into electricity retailing in Tasmania. A number of existing electricity retailers in the NEM also told the Expert Panel, in submissions and at public hearings, that their interest in participating in the Tasmanian electricity market would be severely diminished, or non-existent, under this model and unless the risks to them from Hydro Tasmania's dominance of the wholesale market was effectively curtailed.
>
> Goanna Energy's "The Final Step report for the TSBC"[6] included the results of an assessment of potential new entrant retailer interest in the Tasmanian market based

5 Tasmanian Energy Reform Market and Regulatory Framework Position Paper, Response from the Tasmanian Small Business Council, March 2013, p28

6 Tasmanian Small Business Council – the Final Step, Moving to full retail Contestability in the Tasmanian electricity market. AP 497, Final Report. January 2013

on a survey of NEM retailers in late 2012. The report found that sufficient retailers were interested in participating in the Tasmanian electricity market to provide a foundation for competition, but that their interest was diminished by two things in particular:

- The existing wholesale market arrangements (i.e., the dominance of Hydro Tasmania as a generator and the unacceptable degree of risk this entailed for them); and
- The continued regulation of retail prices for small customers

On the other hand, it can be gleaned from both the Expert Panel and Goanna's report that retailer interest in participating increased under reforms which introduced competition into the wholesale market as this provided a more level playing field and lowered risk exposure. This was particularly so if they gained access to a generation portfolio which allowed them to better manage the inherent risks of participating in the Tasmanian electricity market (e.g. hydrological, import constraints, small size).

The flaws in the Government's wholesale reforms were themselves therefore probably serious enough to dissuade retailers from seeking to acquire Aurora's retail base. This combined with the small size of the market would have almost certainly been a 'show stopper' leading to the failure to successfully prosecute the sale of Aurora's retail base."7

The TSBC remains strongly of the view that competition in Tasmania's wholesale electricity market is an essential pre-requisite for genuine retail competition, with the associated reduction in retail electricity prices, and re-affirms its previous concern about the Government's divergence of views from the Expert Panel advice, and from what it believes is the overwhelming body of evidence, in addition to the comprehensive arguments put forward by the Expert Panel, in support of establishment of a wholesale electricity market in Tasmania.

The TSBC notes that in rejecting the Panel's advice on wholesale competition, no comprehensive analysis of the rationale for that decision was provided. An analysis

7 Tasmanian Economic Regulator, Proposed Changes to the Interim Price- Regulated Electricity Retail Service Price Determinations & Draft Electricity Wholesale Contract Guideline, TSBC submission, November 2013, p12

undertaken by the Department of Treasury and Finance[8] of a three entity trading model versus the Government's chosen regulatory model, produced *after* the Government's decision, offers the only insight into that decision. The TSBC's notes the timing of that analysis and considers it to be significantly inferior to the comprehensive analysis, including peer review, undertaken by the Expert Panel.

Accordingly, the TSBC strongly recommends that the current government reverse the decision of the previous government and proceed to implement the competitive wholesale market model as proposed by the Expert Panel. After such a decision is implemented, it can be expected that retailers will choose to enter the retail market, allowing existing retail regulation to be phased out, once an assessment of that market indicates that it is no longer necessary.

The TSBC contends that further consideration of the existing regulatory framework, in the absence of wholesale competition, would add little or no value, given previous submissions on this topic, and would merely be tinkering at the edge.

The TSBC also notes however that a greater focus by the Government on the efficiency of the network businesses (now TasNetworks) is appropriate, and addresses that issue in its response to Question 4 of the Issues Paper.

Summary – question 1 and TSBC response

What enhancements could be made to regulatory frameworks to ensure the right incentives for businesses and consumers are in place?

TSBC response:

Any further refinements to the existing regulatory framework, in the absence of an effective wholesale market, would add little value and would constitute tinkering at the edge.

TSBC notes the government's 2012 decision to not accept the recommendations of the findings of the Independent Review of the Tasmanian Electricity Supply Industry, against input and advice from a range of sources including the TSBC.

TSBC strongly recommends the government reverse that decision and progress to a competitive wholesale electricity market, which it expects will lead to effective retail competition and ultimately obviate the requirement for regulation of retail electricity prices.

8 Analysis of the Tasmanian Greens' proposed wholesale market model in response to the Expert Panel Final Report, Report to Government October 2012

Question 2

Given both the State and Commonwealth Government are committed to reducing red and green tape, and that the electricity market is highly regulated and complex, what opportunities are there to reduce or remove regulation?

TSBC response

As noted in the response to question 1, the TSBC's view is that the current need to regulate both the wholesale energy market in Tasmania and retail prices would be avoided in the medium term if it reversed its 2012 decision to reject the findings of the Independent Review of the Tasmanian Electricity Supply Industry in relation to the wholesale market structure in Tasmania[9].

Such a reversal would remove the considerable cost burden currently imposed on the electricity supply value chain in Tasmania as a result of the need to regulate wholesale and retail prices, translating to lower electricity prices for small business customers and all other customers.

The cost of (economic) regulation of wholesale and retail electricity prices was $0.6M in the 2012/13 financial year.[10]

The TSBC welcomes the opportunity to put its case to the Government, the Department or the Energy Working Group, noting that it believes the case for adopting the Expert Panel findings has already been well argued by us and other key stakeholders.

The TSBC strongly endorses the need to reduce red and green tape but from past observations of governments (federal and state) attempting to achieve that objective there have been very few examples of success. Accordingly the TSBC suggests that success will be achieved by setting clear, measurable time bound targets, identifying the steps and timing to achieve the targets, identifying accountabilities, holding people accountable for delivery, and publicly reporting progress.

9 Electricity Supply Industry Expert Panel, An Independent Review of the Tasmanian Electricity Supply Industry, March 2012

10 TASMANIAN ECONOMIC REGULATOR, ANNUAL REPORT, 2012-13, p35

Summary – question 2 and TSBC response

Given both the State and Commonwealth Government are committed to reducing red and green tape, and that the electricity market is highly regulated and complex, what opportunities are there to reduce or remove regulation?

TSBC response:

TSBC strongly recommends the government should reverse the 2012 decision to reject the findings of the Independent Review of the Tasmanian Electricity Supply Industry in relation to the wholesale market structure in Tasmania.

Such a reversal would remove the considerable cost burden currently imposed on the electricity supply value chain in Tasmania as a result of the need to regulate wholesale and retail prices, translating to lower electricity prices for small business customers and all other customers.

The TSBC welcomes the opportunity to put its case to the government, the Department or the Energy Working Group.

Question 3

Is retail competition important because of price, choice or for other reasons?

TSBC response

Small business keenly awaits the arrival of genuine competition into electricity retail sales in Tasmania, and the TSBC notes that the introduction of full retail contestability on 1 July 2014 occurred 12 years after its introduction in Victoria, and that small businesses in every state served by the National Electricity Market (NEM) now enjoy the benefits of full retail competition.

Since the introduction of FRC in Victoria in 2002, successive Tasmanian governments have been provided with a vast body of evidence on the relative merits of competition in the electricity sector (including the introduction of competition to elements of the monopoly, regulated network components), and have indicated their commitment to electricity retail contestability.

Evidence of the importance of competition in delivering optimal price and service outcomes is well documented as part of the vast body of evidence noted above, and is the basis on which small business is founded. Small businesses must deliver a service valued by customers (that is, with the right mix of price and quality, for products and services) and if they fail in that endeavour will be forced out of business because of competition from other businesses offering lower prices and/or better service.

There is no substitute for competition in terms delivering optimum price and quality outcomes. Giving customers choice gives them power, which is appropriately reflected in the title of the Australian Energy Market Commission's Power of Choice review[11], which focussed on providing information to electricity customers to make choices about how they use electricity.

In short, choice is synonymous with competition and improved price and service outcomes. For small business choice of electricity retailer has the added benefit of product choice. Retailers will provide different packages for consideration of small business customers, as part of competitive product differentiation strategies, therefore small businesses would be in a position to select the package which best suits their business needs. Competition would also see the entry of other providers offering services such as energy efficiency, energy management services, bill interpretation and management and load management.

11 AEMC FINAL REPORT, Power of choice review - giving consumers options in the way they use electricity, 30 November 2012

The TSBC notes the reference in the Department's Issues Paper, to which this submission responds, at page 15:

> *"In a mature, competitive market, multiple participants would be expected to provide downward pressure on prices through ensuring their cost structures are as efficient as possible to compete with one another."*

The Hilmer review of national competition policy, which guided the development of a nationwide process of competition reform, suggested:

> *"As with the structural separation of natural monopoly elements from potentially competitive elements, however, reforms of this kind may be resited by incumbents or, in some cases, owning governments. Accordingly, any more systematic approach to this question should place emphasis on rigorous, open and independent analysis."*[12]

The Expert Panel Independent Review of the Tasmanian Electricity Supply Industry, which was commissioned by the previous government and which reported in March 2012, delivered the rigorous, open and independent analysis suggested by the Hilmer report, with the terms of reference including:

> *Looking forward, what policy, regulatory, governance and structural reform options could be considered to underpin the efficiency of the sector in the future and how should these be evaluated and prioritised?*[13]

The Expert Panel's final report included, at section 7, a review of the merits of retail competition in the Tasmanian context, including at page 69 a comparison of price diversity in the NEM regions, indicating that the development of competition provides the path for offers to customers that are materially below regulated prices.

The TSBC does not propose to restate the body of analysis of the benefits of competition provided in the Independent Review, with which policy makers and the Department would be well familiar, other than to suggest that the arguments for full and effective retail competition provided by the review are compelling, and are in accordance with the views and firsthand experience of Tasmanian small business.

The link between structural changes in the Tasmanian wholesale electricity market and the benefits of effective retail competition are, in the TSBC's view, also spelled out in unambiguous and compelling terms in the Expert Panel's final report, and are well familiar to policy makers and the Department.

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12 National Competition Policy, NATIONAL COMPETITION POLICY REVIEW, 25 August 1993, p225

13 Electricity Supply Industry Expert Panel, An Independent Review of the Tasmanian Electricity Supply Industry, Final Report, Volume 1, March 2012, page i

The TSBC notes however one reference, at page vii:

> *"Simply put, the Panel considers that a failure to address the current wholesale energy market structure would effectively 'lock in' an absence of effective competition and customer choice indefinitely, denying Tasmanian small businesses and households the clear benefits of competition and choice that have been delivered to consumers elsewhere in Australia".*

The TSBC has previously submitted, in its response to the Tasmanian Energy Reform Market and Regulatory Framework Position Paper, that:

> *"The TSBC recognises the critical role that the wholesale market plays in Tasmanian electricity reform. It does not, however, agree with the Government's view that the Tasmanian hydro-electric system necessarily needs to be run as if it were a natural monopoly. It therefore does not accept that regulation of the wholesale electricity market is the best approach to reform. Following its extensive (and expensive) investigation, the Independent Panel certainly did not think so, opting instead for a solution involving wholesale competition and dismissing the regulatory approach as inferior.*
>
> *The TSBC is concerned both about this divergence of views and that the Government's choice may constrain retail competition"*[14]

The TSBC believes the failed attempt to sell Aurora's customer list is a clear demonstration of the market confirming the Expert Panel's findings and recommendations concerning the need for wholesale market reform in order to deliver effective retail competition. Those findings and recommendations are in accordance with the views of the TSBC.

Research commissioned by the TSBC[15], undertaken by Goanna Energy who conducted interviews with six national electricity retailers, before the failed attempt to sell Aurora's customer list, provided further confirmation of the need for wholesale market reform, and the Panel's findings and recommendations. A key outcome from that research was:

> *"Factors which reduce business appetite to participate in the Tasmanian Market.*
>
> *Only one retailer, the currently active ERM Business Energy, reported no factors reducing their appetite to participate in the Tasmanian market. Each and all of the*

14 Tasmanian Energy Reform Market and Regulatory Framework Position Paper, Response from the Tasmanian Small Business Council, March 2013, p28

15 Tasmanian Small Business Council, The Final Step: Moving to full retail contestability in the Tasmanian electricity market, FINAL REPORT, January 2013

other five retailers interviewed reported factors in the Tasmanian market which act to reduce their business appetite. These factors included:

- *Small relative Market size*
- *Ability to understand and manage spot market volatility.*
- *Ability to access OTC (Over The Counter) swaps & Caps to manage portfolio risk.*
- *Limited wholesale market liquidity (is the biggest factor). (emphasis added)*
- *Retail price regulation.*
- *Lack of counterparties in wholesale market to trade risk management products.*
- *Wholesale market conditions.*
- *Ownership structures.*
- *Regulatory arrangements.*
- *Threat of Hydro Tasmania competing in the market – potentially via Momentum*
- *Low level of customer experience with innovative products*

Along with the small market size, a theme of the uncertainty, particularly related to the wholesale market and retail price regulation, was often repeated in the interviews as a negative market assessment."

The TSBC is firmly of the view that the Government should move, as soon as possible, to implement the recommendations of the Expert Panel relating to wholesale market reform, in order to facilitate genuine retailer interest in the Tasmanian electricity retail market, thus genuine competition, as a matter of priority.

If the Government wishes to maintain the current regulated wholesale market arrangements, contrary to the advice of the Expert Panel, the TSBC and other key stakeholders, then the TSBC believes the Government must acknowledge that genuine retail competition will not occur, and it should avoid fostering the perception that it will occur at some point in the future.

Tasmania would then be the only NEM state not to have retail competition and small business can then make their own decisions about how that will impact their competitiveness, and make their business plans accordingly. That would be a better outcome than to wait with the perpetual promise of an outcome that will not actually occur.

Summary – question 3 and TSBC response

Is retail competition important because of price, choice or for other reasons?

TSBC response:

Choice (who we buy a product or service from) is synonymous with competition. Giving small business customers the choice of who they contract with to buy electricity will drive the beneficial outcomes associated with competition – improved price and/or service quality.

The Electricity Supply Industry Expert Panel review provides a comprehensive analysis of the merits of electricity retail competition in the Tasmanian context.

It also highlights unequivocally that reform of the existing wholesale market arrangements is a necessary precursor to the successful introduction of electricity retail competition.

The failed attempt to sell Aurora's customer list is a market confirmation of the advice provided by the expert panel.

As in its response to question 1, TSBC strongly recommends the government reverse the decision of the previous government in relation to wholesale market reform and progresses to a competitive wholesale electricity market, which it expects will lead to effective retail competition.

Question 4

What enhancements or additional information could increase the reporting transparency of the Government's electricity businesses and contribute to improved efficiency?

TSBC response

The TSBC notes the reference in Question 3 to the provision of additional information to contribute to improved efficiency, and also notes the reference in the Issues Paper body to Chapter 6 of the expert Panel Review[16], dealing with governance reform.

The TSBC is of the view that the Expert Panel's analysis and conclusions in Chapter 15 of Volume 1 (including efficiency and effectiveness) and Part C of Volume 2 (A review of the efficiency and effectiveness of the State Owned Electricity Businesses) must be considered alongside Chapter 6, and notes the comprehensive analysis provided, and the robustness of the Panel's conclusions and recommendations.

The TSBC notes and endorses:

- The 6 recommendations at Section 6.8, Volume 1 (way forward – governance);
- Findings in relation to efficiency (Section 15.2.4, volume 1); and
- Findings in relation to efficiency (Part C, Volume 2).

The TSBC suggests the Government should progress the recommendations at 6.8, repeated below for completeness, as a matter of priority.

- *1. The Tasmanian Government develops a publicly-available Energy Business Ownership Policy to more clearly articulate its overarching strategic objectives and scope for the SOEBs.*
- *2. The Tasmanian Government transparently identifies, endorses, costs and funds all non-commercial activities undertaken by the SOEBs, consistent with its existing CSO policy framework. CSOs should be directly funded through the budget process, rather than through internal transfers and acceptance by the Shareholders of reduced rates of return.*
- *3. SOEB oversight continues to be refined and improved over time with a specific focus on putting in place accountability and incentive mechanisms that provide a clearer 'line of sight' between Shareholder expectations and the requirements of the regulatory framework on the one hand, and board, management and staff performance on the other.*

16 An Independent Review of the Tasmanian Electricity Supply Industry, Final report, March 2012

- *4. The following key functions should underpin any Government review of allocation of energy market and policy responsibilities across the bureaucracy:*
    - *A strong SOEB ownership and oversight function, focused on driving the efficient performance of the businesses from a Shareholder perspective;*
    - *An expert energy policy function with the sufficient mandate, capacity and authority to provide robust advice to Government, preferably through the portfolio Minister; and*
    - *A strategic, 'whole of government' policy oversight capacity with the ability to weigh and consider the impacts of energy policy proposals from a more holistic perspective, taking into account broader social, economic and environmental impacts, preferably coordinated by a central agency.*
- *5. At a minimum, each of the SOEBs provides to the Parliament – and therefore the wider Tasmanian community – the following:*
    - *An annual Statement of Corporate Intent (SCI) at the commencement of the Financial Year, summarising the key objectives and performance targets from the SOEB's Corporate Plan;*
    - *A Half-Yearly Report that provides a summary of year-to-date performance against targets set in the SCI; and*
    - *An Annual Report.*
- *6. The TER is given the discretion to independently apply appropriate approaches and methodologies, within the context of principles and objectives set by the regulatory framework. If there are specific outcomes that the Government considers should be taken into account, then it may put the case to the TER in submissions to the independent regulatory process.*

In addition to the above recommendations, the TSBC adds the following:

1. As discussed in the introduction to this submission, the TSBC endorses the development of a comprehensive energy strategy. In order to ensure the strategy is well considered; well-constructed and robust; identifies long term objectives; spells out the actions required to deliver the objectives; includes appropriate targets and measurement mechanisms; and there is appropriate oversight of progress, the TSBC considers that a properly resourced policy function within Government is essential. That view accords with recommendation 6.4 above, however the TSBC notes that whilst there is a Minister for Energy and State Growth (Matthew Groom), there is currently no Energy division to support the energy portfolio, a situation which does not accord with energy policy and energy matters being a significant issue for Government, and one which needs to be addressed, as part of the implementation program, if the Energy Strategy is to be given meaningful life.

2. The Issues Paper identifies that network costs make up the largest component of Tasmanian electricity prices, at 58.9%. Network prices (transmission and distribution) are determined via the extensive regulatory process administered by the Australian Energy Regulator (AER). The National Electricity Objective, National Electricity Law, National

Electricity Retail Law, and National Electricity Rules which underpin that process have a strong focus on efficiency, reinforced by recent reforms, and electricity network service providers are required to demonstrate the prudency and efficiency of all operating and capital expenditures. National and international benchmarking of those expenditures, against a range of financial and non-financial measures, is a key determinant of expenditures allowed by the AER.

The TSBC is of the view however that despite the rigour of the AER's processes, expenditures allowed to date have not been efficient, due to the inflation of costs, beyond an efficient level, which is inherent in almost all of the network businesses' cost bases, and therefore benchmarking data.

Transend's (TasNetworks) Revenue Proposal submitted to the AER in May 2014 included a benchmarking analysis undertaken by Huegin Consulting Group[17]. The analysis of eight operating and capital expenditure productivity indices at page 15 shows that of the five transmission service providers included in the analysis (Transend, Transgrid, Electranet, Powerlink, SP Ausnet) the privately owned, Victorian SP AusNet, (now AusNet Services) outperformed the other providers on all eight measures. The TSBC suggests that outcome is driven by a number of factors which are reflected in the recent revelations of Mr Vince Graham, Chief Executive Officer of Networks NSW, as reported in the "Australian" newspaper on Wednesday 20th and Saturday 23rd August 2014.

The Australian quoted Mr Graham as indicating that union power, public ownership and "amenable management" had driven higher electricity prices. The TSBC holds that from its involvement with AER network regulatory process, including the 'Better Regulation' program and the current TasNetworks review, Mr Graham's points also hold true in Tasmania. Moreover, the interactions our members have with past and present employees and contractors to both Transend Networks and Aurora Energy (distribution) suggest there are substantial opportunities to reduce costs in both businesses (now TasNetworks), by focussing on work practices, works delivery processes and resource levels.

TSBC therefore proposes that as part of the reporting requirements suggested by the Expert Panel, at recommendation 5 of Section 6.8 above, the Government should require TasNetworks to report against a range of KPIs which reveal underlying efficiency, in addition to those which are included in revenue proposals submitted to the AER. Those KPIs could include, for example:

- overtime earned to total earning for field staff;

17 Tasmanian Transmission Revenue Proposal, Regulatory control period 1 July 2014 – 30 June 2019, 31 May 2014, Appendix 5

- value of allowances paid compared to total salaries;
- utilisation factor of distribution and transmission lines and substations;
- utilisation factor of heavy plant;
- percentage of rework to total work completed; and
- percentage of work constructed as specified, as designed.

Reporting of TasNetworks activities, including via a public reporting process, such as that employed by the Tasmanian Energy Regulator in the Annual Energy Performance Report[18], in addition to normal Board and shareholder reporting, should include improvement targets for those measures and regular reporting of progress towards the improvement targets.

3. The Expert Panel Report comments on instances where the Government's desire to keep the state owned electricity businesses as financially whole as possible, in some cases at the expense of electricity consumers. An example is:

> *"Under the 2007 Determination - where the Government, not the TER, set the wholesale energy cost allowance - one of the key principles applied by the Government was that the allowance should contribute to the sustainability of Hydro Tasmania and Aurora Energy to ensure sufficient revenue capacity to earn a commercial return. This ultimately resulted in an 'adjustment factor' of approximately $3MW/h being applied to the allowance that had been recommended by independent consultants based on the application of a long-run marginal cost methodology."*[19]

Similarly:

> *Currently, non-contestable customers and Hydro Tasmania are carrying the financial burden of the costs of having the TVPS available as 'supply reliability insurance'. This is unlikely to be a sustainable approach under typical inflows and storages conditions (in terms of Hydro Tasmania's willingness to contract with thermal generation to manage hydrological risk) and these arrangements will not be robust with a move to market-based arrangements for all customers. The financial position of the TVPS in the context of prevailing market conditions is a key issue that needs to be resolved as part of the Tasmanian Government's future Energy Strategy*[20]*.*

18 Office of the Tasmanian Energy regulator, Energy in Tasmania Performance Report

19 P63, Volume 1

20 P74, Volume 2

The TSBC strongly endorses the Expert Panel's position on such instances and the Panel's recommendations at Section 6.8 of its report noted above (1, 2 and 6), with the expectation that small business pays an appropriate share of efficient energy costs and is not forced to pay for electricity at a price which incorporates what amounts to hidden and substantial economic subsidies.

4. The TSBC provided a submission to the Tasmanian Economic Regulator in response to its Consultation Paper on proposed changes to the Interim Price-Regulated Retail Service Price Determinations in November 2013.[21]. The TSBC submission recommended the following:

> *6. The TER should review all aspects of the building blocks in its previous Determinations given the severe time constraints it was under, its inability to consult adequately with stakeholders, including small consumers and its apparent inability to verify certain significant information provided by the Government and the Department of the Treasury.*
>
> *7. The TER should provide a retail margin to Aurora at, or close to, the 3.8 per cent which was provided to Aurora under the 2010 Determination, as this would be more appropriate to the weak competitive environment Aurora is likely to face, at least until there is evidence that Aurora will indeed face increased competition in future.*
>
> *8. The TER should provide no allowance for customer acquisition and retention costs (CARC) in its revised Determination for Aurora on the basis that it is far from certain that Aurora will face sufficient competition in future to justify such an allowance.*
>
> *9. Given the impacts of our Recommendations 7 and 8 above are material in that they would result in an estimated $37.5 million reduction in Aurora's notional maximum revenue (NMR) over the period of the Determination, the TER should amend the Determination to account for this.[22]*

The Tasmanian Regulator did not agree with the TSBC's recommendations and determined that the retail margin and customer acquisition and retention costs would remain essentially as proposed in the consultation paper. The implication of that decision is that non contestable customers will pay, over a 2.5 year period from 1 January 2014, around $37M representing the costs Aurora will incur in seeking to preserve its market share, against competing retailers. Given the absence of retailers genuinely competing and the likelihood

21 TSBC submission, Proposed Changes to the Interim Price- Regulated Electricity Retail Service Price Determinations & Draft Electricity Wholesale Contract Guideline, November 2013

22 Ibid, p20

of that situation prevailing, the TSBC finds the imposition of that cost and the share applicable to small business to be unjustified and not representative of efficient costs.

The TSBC therefore proposes that Aurora should be compelled to report on the actual costs it incurs in its role as the Regulated Offer Retailer (ROR), resulting from the entry into the retail market by an active competitor, and the actual costs it incurs as a result of its customer acquisition and retention activities, compared to the allowances made in the final changes to the interim price-regulated retail service price determinations.[23]

The TSBC further proposes that a mechanism be established to return any over recovery of those costs to domestic and small business customers.

Summary – question 4 and TSBC response

What enhancements or additional information could increase the reporting transparency of the Government's electricity businesses and contribute to improved efficiency?

TSBC response:

The TSBC:

. Notes and endorses the conclusions and recommendations of the Electricity Supply Industry Expert Panel Review at Chapters 6 and 15 of Volume 1 and Part C of Volume 2.

. Suggests the government should progress the recommendations at Section 6.8 as a matter of priority.

. Proposes a number of key performance indicators applicable to TasNetworks which should be included in the proposed reporting regime, targeted at improving efficiency in areas where it believes there is currently substantial inefficiency.

. Strongly suggests small business pays an appropriate share of efficient energy costs and is not forced to pay for electricity at a price which incorporates what amounts to hidden and substantial economic subsidies.

. Proposes that Aurora should be compelled to report actual costs against allowed costs of activities resulting from the entry of new retailers, and that a pass back mechanism be developed for any over recovery.

23 Tasmanian Economic Regulator, Report on the investigation of maximum prices for interim price-regulated electricity retail services for small customers on mainland Tasmania, July 2013.

Question 5

Do energy intensive and trade exposed businesses require greater future price certainty to maintain and/or grow their operations?

TSBC response

The TSBC recognizes and acknowledges the need for large, energy intensive electricity consumers to have long term certainty over significant input costs, to the greatest extent possible. The TSBC notes the significance of transmission price increases in the past five years which would not have been contemplated in the business planning of those large, energy intensive customers, but further notes that small business has also seen significant increases in transmission costs over that period, as part of total electricity network costs, and is concerned to ensure that no effort to stabilise transmission price increases for major industrial (MI) customers translates to an adverse impact on small business.

The TSBC notes that in relation to Transend Network's (now TasNetworks, transmission) Transitional Revenue Proposal only three submissions were received from the public – from the TSBC, the National Generators Forum and the Major Energy Users, suggesting that in the public discussion of rising electricity prices, the transmission component does not feature prominently.

In its submission, the Major Energy Users (MEU) suggested[24]:

> *"…… it must be recognised that transmission costs can be a significant element of a consumer's bill, as the closer a consumer is to the transmission supply point and the larger the demand of the consumer, the more significant transmission costs can become. In fact, MEU members have seen transmission charges increase by >200% over the last 5 years! This has come against a backdrop of a continuing high currency rate exchange and tough trading conditions for trade exposed businesses. The issue that needs to be addressed is not the share of the electricity bill but the quantum of the increase. No MEU member has reported any other element in their cost structure that has risen by the amounts claimed by Transend. It is, therefore, essential that*

24 Submission to the Australian Energy Regulator on Tasmanian Electricity Transmission Revenue Reset, Transend, Application for Transition Year 2014/15, A response by the Major Energy Users Inc. February 2014, p8

transmission costs are not treated as insignificant, and are addressed in a comprehensive manner."

The regulatory process for establishing annual revenue requirements for transmission (and distribution) network service providers essentially involves an allowance for return on and return of capital (based on the total value of assets) and an allowance for operating expenditure. Increases in capital expenditure over and above return of capital (depreciation) will result in increased total assets, which will result in higher transmission prices, as will increases in annual operating costs, on the basis that electricity consumption remains flat. Prices will increase further in the event that electricity consumption falls.

Transend's Regulated Asset Base (RAB) is projected to grow from $951.4M in 2009/10 to $1,412.9 in 2013/14, an increase of $461.5M or 33%.[25]

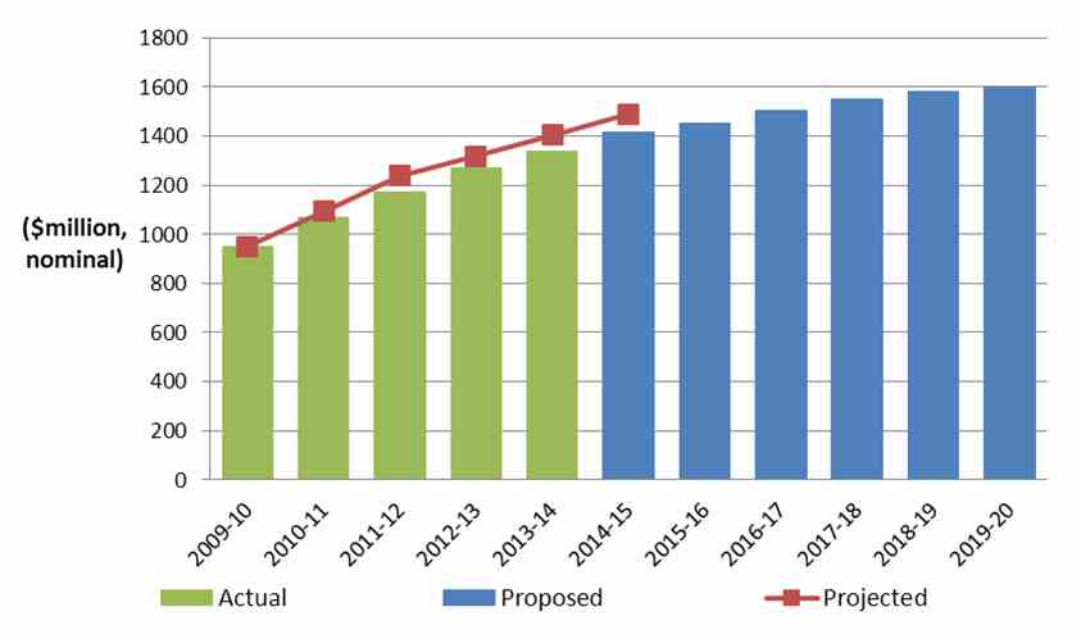
The major driver for that increase, which flows directly into Transend's maximum allowable revenue and thus prices, is the excess of allowed capital expenditure ($563.5M) over depreciation ($272.6M), coupled with inflation on the regulated asset base of $152.6M over the period[26]. In an economic environment where demand for electricity has been falling, the existence of such a large difference between the two is difficult to reconcile, further exacerbated by the fact that Transend's actual capital expenditure as noted above was less than allowed by the AER in its 2009 revenue determination.

Figure 1 below shows the increase in the value of Transend's regulatory asset base for the five years to 2013/14, together with the projection to 2019/20:

25 TasNetworks, Tasmanian Transmission Revenue Proposal, Regulatory control period 1 July 2014-30 June 2019, 31 May 2014

26 Ibid

Figure 1 Transend opening RAB from 2009–19 ($m, nominal)

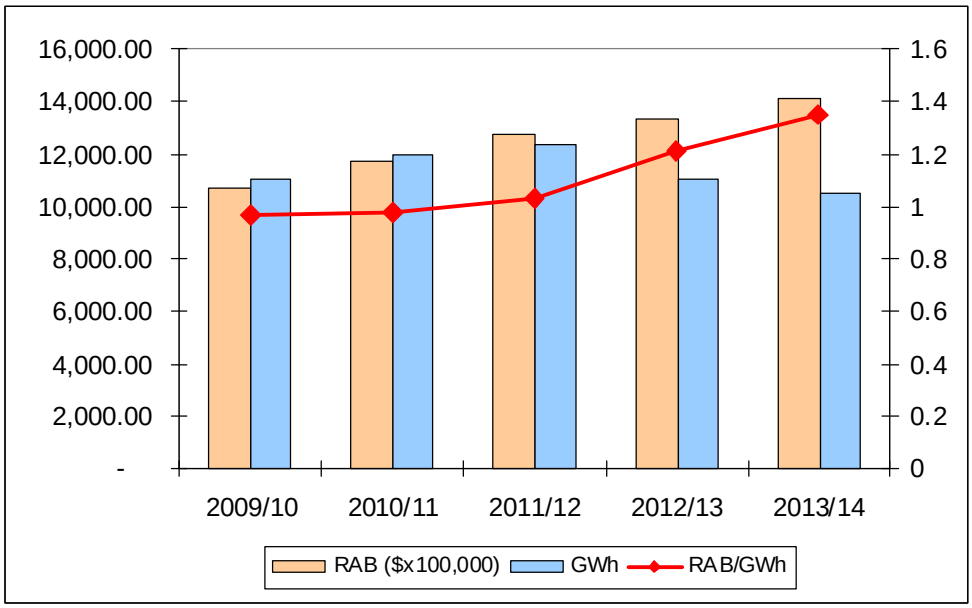


Source: Transend TRP (transitional revenue proposal) and AER analysis[27].

The price impact associated with the increase in asset value is reflected in figure 2 below – the value of the asset base compared to energy sales.

27 AER TransGrid and Transend Transitional transmission determinations, 2014–15, March 2014

Figure 2 Transend regulated asset base (RAB) to total energy sales



Source – TasNetworks annual report 2012/13, Transend Revenue Proposal May 2014
(2013/14 GWh projected, assuming 5% reduction)

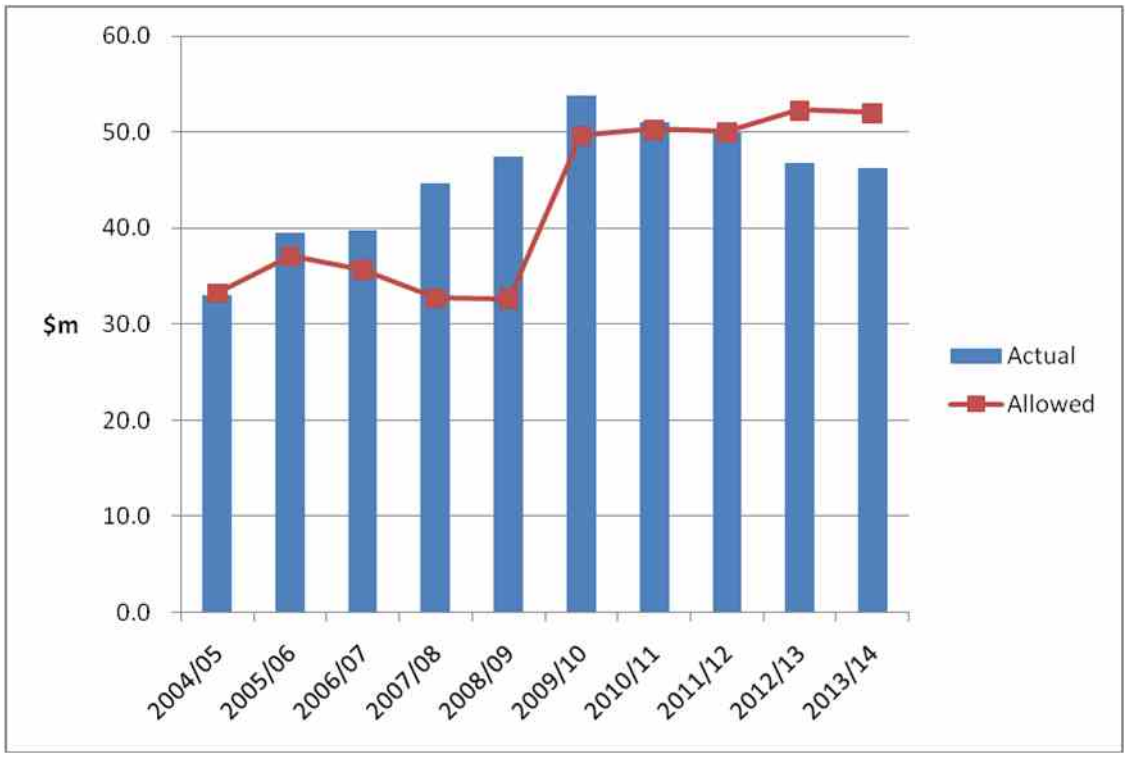
Figure 2 identifies that the value of transmission assets used to deliver electricity to all Tasmanian homes and businesses has increased, whereas total demand for electricity has fallen. Given the mechanisms which allow transmission network service providers (TNSPs) to recover their allowed revenues, the shape of the line in figure 2 would be expected to be, and has been, reflected in unit price increases. The TSBC acknowledges that the relative scale and impact of those price increases is much greater for MIs than for small business and domestic customers, where transmission price increases have been blurred by increases in the cost of other components of the electricity value chain, including wholesale energy, green schemes including the carbon tax, distribution and retail components, however the increase in transmission prices to small business has also been significant.

[The TSBC notes the earnings associated with inter-regional transmission use of system (TUOS) charges and the value of those charges flowing to Tasmania during periods of export of electricity from Tasmania. The TSBC suggests there is an opportunity to review the benefits sharing of those charges and how they flow back to small business.]

A second driver of transmission price increases arises from increases in operating expenditure, where any increase year on year passes directly to allowable revenue, and hence transmission price increases. Figure 3 shows the increases in Transend's operating

costs over ten years, as presented in the TSBC submission to the AER on Transend's 1 July 2014 to 30 June 2019 Revenue Proposal[28].

Figure 3 Transend – operating expenditure.



Source – TSBC submission to AER, August 2014

The increase in operating expenditure, as with the increase in Transend's regulated asset base, is not matched by an increase in total electricity demand over the period shown. Increases in the asset base, coupled with increases in operating cost, therefore translate directly to increased transmission prices.

In response to the MEU's submission to the AER noted above, Transend indicated in its response to stakeholder submissions:

> *"We note that the MEU has identified a number of aspects of the pricing methodology that it regards as anomalous. Our pricing methodology proposal explains that we have complied with the Rules and AER Guidelines. The resulting prices should therefore be regarded as 'fair'.*

28 TSBC Submission to the Australian Energy Regulator on TasNetworks Transmission Revenue Proposal, 2014/15 to 2018/19, August 2014

We acknowledge MEU's concerns and we would be pleased to engage in discussions regarding a future Rule change proposal. It is important to recognise, however, that transmission pricing is necessarily imperfect and any change will create 'winners' and 'losers'."[29]

The methodology for translating Transend's (now TasNetworks, transmission) allowable revenues into customer prices is extremely complex. At each revenue determination, Transend, as with all transmission network service providers, is required to submit a "pricing methodology", which is approved or otherwise by the AER as part of the determination process under Chapter 6A of the National Electricity Rules and the AER's pricing methodology guidelines.

Transend's pricing methodology was approved by the AER in its April 2009 decision on Transend's transmission determination for 2009/10 to 2013/14 (minor changes are proposed for the 2013/14 to 2018/19 determination period).

A very high level representation of that methodology is shown at figure 4 below.

It is beyond the scope of this submission to undertake a detailed analysis of Transend's pricing methodology and how the increases in asset base and operating costs flow through to transmission prices for various customer classes, including MIs. The TSBC points out however that Transend's response to the MEU's concerns, noted above, indicates that it believes it has complied with the requirements of the National Electricity rules, and that any change would create winners and losses.

It is the TSBC's view that this is an extremely important issue, not just to MEU members but equally to small businesses who may be adversely impacted by any change. Accordingly the TSBC proposes that the Department undertake a review of Transend's Pricing Methodology, with appropriate consultation and active engagement with all key stakeholders.

The TSBC notes that Transgrid issued a consultation paper on transmission pricing in November 2013, as part of the review of its Pricing Methodology for its upcoming regulatory control period[30] Transgrid indicated that *"whilst this was not a requirement of the regulatory process it is an issue of high importance for consumers"*[31].

The TSBC suggests that the Department might use Transgrid's approach as a guide to undertaking the proposed review and notes the review should encompass the following:

29 Appendix 2,Transend response :Stakeholder submissions to our transitional Revenue Proposal, May 2014.

30 Appendix AH Transmission Pricing Methodology – Better Outcomes for Customers

31 Transgrid, Transitional revenue proposal 2014/15

- The cause of perceived anomalies in the application of Transend's pricing methodology.
- A full assessment of the impact of any proposed changes on small business customers.
- Consideration of the use of the rule change mechanism (changes to the National Electricity Rules) to give effect to any proposed changes to the pricing methodology;
- A comprehensive assessment of the impact of a continuing downward trend in total electricity demand on transmission prices, should Transend's asset value not be adjusted;
- A comprehensive assessment of the value of Transend's assets, against the accounting "recoverable amount test", in the event that any increase in transmission prices flowing from a reduction in total electricity demand is deemed unacceptable.

Summary – question 5 and TSBC response

Do energy intensive and trade exposed businesses require greater future price certainty to maintain and/or grow their operations?

TSBC response:

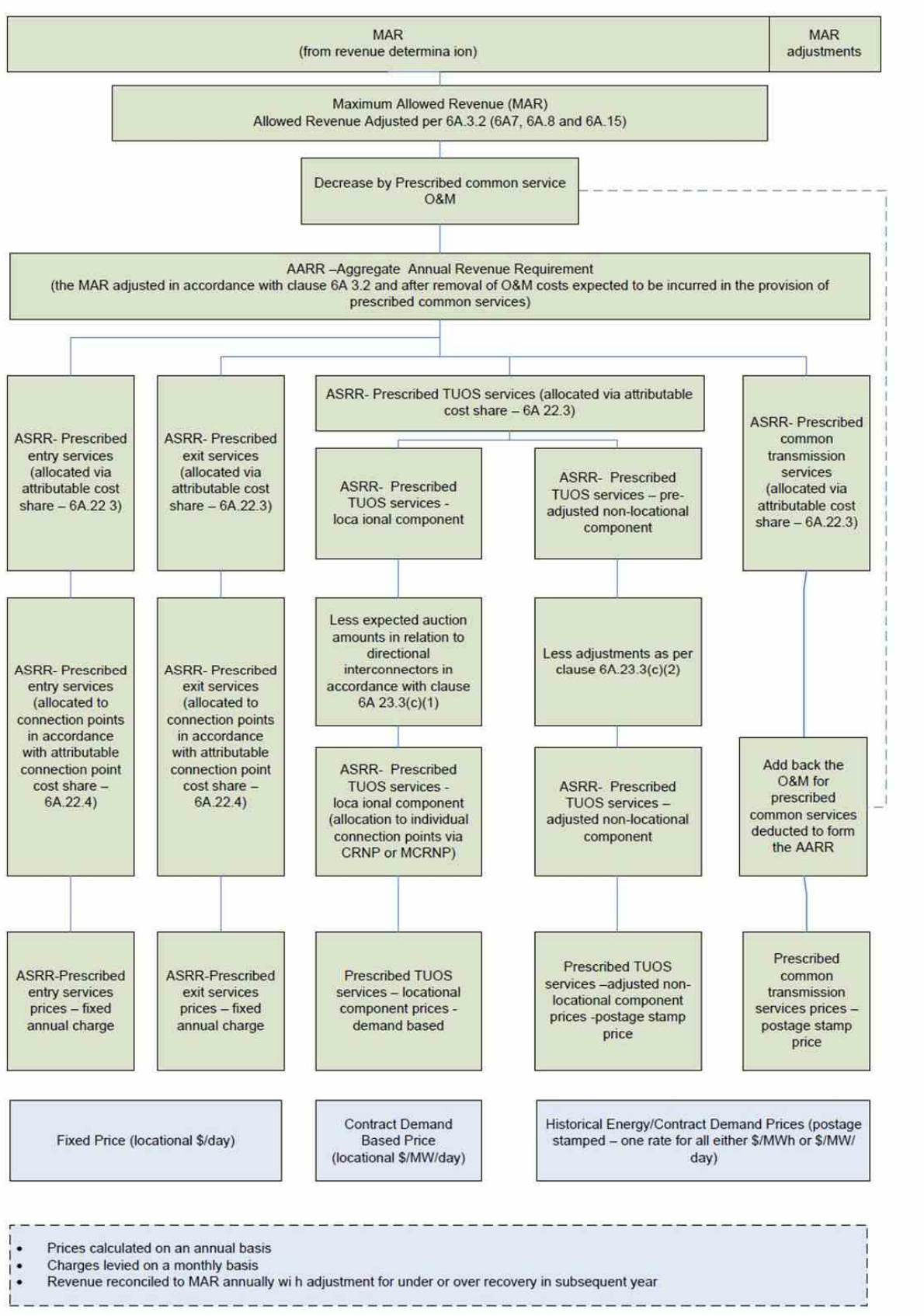
Yes, however the question of price certainty appears to stem from the very substantial increases to transmission prices over the last five years, as flagged by the MEU in its February 2014 submission to the AER.

The TSBC notes that small business has also suffered significant transmission price increases, as well as other increases across the electricity supply chain.

Any change to the Pricing Methodology applied by Transend which reduced transmission prices to MIs would be expected to have an opposite adverse effect on small business.

The TSBC suggests the Department should undertake a comprehensive review of Transend's (TasNetworks) Pricing Methodology, including asset values and load growth projections and the implications for future transmission prices.

Figure 4 Transend pricing methodology



Question 6

Would you consider accepting slightly lower levels of reliability if this resulted in materially lower prices?

TSBC response

Tasmanian small businesses require access to a reliable supply of electricity and those that are connected to natural gas similarly require access to a reliable supply. For most of those businesses any interruption to electricity supply means that the business cannot operate and for a large percentage, lost revenue arising from an interruption to their electricity supply is not recoverable. Similarly, adverse customer perceptions arising from electricity supply interruptions can lead to long term reputation damage with a corresponding negative impact on business performance.

By way of example, any electricity supply interruption at 7.00pm on a Friday evening could cause loss of revenue and reputation damage to a busy restaurant. Several such interruptions over an extended period would invariably result in long term damage. Many small businesses now operate from the owners' premises and most of those rely heavily on internet and telephone access, both of which are dependent on electricity supply and therefore supply interruptions can be severely damaging.

That situation is different to many medium and large businesses where the impact of electricity or gas supply interruptions can be mitigated by, for example, running plant harder, or for longer, and/or requesting staff to work extended hours, once supply has been restored in order to recover lost production.

The percentage of small businesses involved in activities such as supplying quality food produce, such as seafood and fresh fruit, to customers demanding very high quality and very short delivery times, both local and overseas; those involved in provision of IT support services and those providing internet based services is steadily increasing. For those businesses, electricity supply interruptions can be extremely damaging.

Small business dependence on a reliable electricity supply is therefore in general increasing, and those who have chosen gas as a source of energy have invariably done so with very high expectations of reliability of supply. Accordingly the TSBC and its members expect that the reliability of electricity and gas supply will not reduce and will, in keeping with a business environment which demands continuous improvement in product and service quality, also continuously improve. Further, that improvement will come from increased efficiency, not from increased cost.

Against that background, and noting the significant investment in shared distribution and transmission networks and substation assets in Tasmania over the last 15 years, with much

of that investment justified as reliability driven, customers in Tasmania can reasonably expect that those investments will deliver an increased level of reliability of supply over an extended period of time, the TSBC's answer to question 6 as posed in the Issues Paper would be no, however we remain open minded to the scale of the price reduction which would result from any properly assessed and managed reduction in reliability.

We do not however consider that we or our members are well placed to provide other than a subjective response to the question, in the absence of a mechanism to properly assess the value to our businesses lost as a result of a reduction in electricity supply reliability, compared to the offsetting value gained as a result of corresponding price reductions. That assessment would deliver different results for every small business.

The nub of the reliability-cost trade off issue is perhaps best summed up in the Australian Energy Market Commission (AEMC)'s Review of the national framework for distribution reliability[32], as follows:

"Reliability refers to the extent to which customers have a continuous supply of electricity. Distribution networks facilitate the supply of electricity to end use customers within each jurisdiction of the National Electricity Market (NEM). The level of reliability that distribution networks are required to provide affects the level of investment that networks undertake. This ultimately feeds through to the electricity prices paid by customers.

As it would not be cost effective or feasible to remove all potential supply interruptions faced by customers, determining the appropriate level of reliability involves a trade-off between the cost of building and maintaining the networks and the value placed on reliability by customers.

As monopoly services, the price charged for distribution services is regulated. Regulation of reliability complements this price regulation to guard against any incentive for networks to reduce reliability levels in order to increase their profits."

TSBC believes that the need to seek an answer to question 6 in the Issues Paper has now been superseded by work in the national regulatory arena.

The trade-off between on the one hand the cost of producing and delivering electricity, and on the other reliability of supply, has been the subject of recent and extensive attention, at a national level, by the Council of Australian Governments (COAG); the Ministerial Council on Energy (now the Standing Committee on Energy and Resources, SCER); the AEMC; the

32 AEMC, FINAL REPORT, Review of the national framework for distribution reliability, 27 September 2013

Australian Energy Market Operator (AEMO) and the Australian Energy Regulator (AER), and involved extensive consultation with key stakeholders, including customer groups.

That work is described in detail below under the heading "National framework for distribution reliability" below, however in summary the AEMC has developed a framework for setting reliability targets which takes account of how electricity network costs vary with different levels of reliability and matches the expected costs of investments against the value that customers place on reliability (value of customer reliability – VCR) and the probability of interruptions.

Implementation of the framework is proposed to be in five stages – an interim stage to develop the supporting arrangements, and four stages to apply the national framework. The timeline for full implementation, on the basis that relevant government bodies such as COAG and SCER adopt the framework as proposed, could be expected to be several years, however each jurisdiction (including Tasmania) can choose to progressively adopt parts of the framework.

Of particular relevance to question 6 in the Department's Issues Paper and the TSBC and members is the following extract from the interim stage program:[33]

> *"The purpose of this Interim Stage is to establish common definitions for expressing distribution reliability targets and to apply the VCR measures reviewed and updated by the AER (but initially developed by AEMO) to facilitate the setting of reliability targets in a manner consistent with the recommended framework".*

The question of what value do customers place on reliability, or the negative value of interruptions, would be determined by the AER, in consultation with industry groups and jurisdictions.

TSBC welcomes the opportunity to contribute to the consultations and industry working group, as proposed in the framework's interim stage implementation plan. TSBC notes however that its members are generally "time poor" and therefore the consultation with and involvement of small business representatives will need to be well managed and focussed to ensure engagement does not diminish or become ineffective.

It is the TSBC's view that the Tasmanian Energy Strategy should recognize and incorporate the work currently in progress at national level concerning the reliability-cost trade off, which has to date involved substantial customer and stakeholder consultation, which will continue, and will deliver a mechanism whereby nationally consistent reliability standards and the subsequent investment (which translates to price) by electricity entities required to

33 Ibid, p93

deliver the regulated standards are matched to the value, empirically measured, which customers place on the level of reliability they experience.

Further, it is the TSBC's view that the recent merger of Aurora distribution and Transend network businesses will increase further joint cooperation in the network planning and operation areas and therefore increase reliability of supply by focussing more on the existing asset capabilities. A focus on greater network automation and smart grid applications can be expected to enhance supply reliability at the same time as reducing capital expenditures in the transmission network.

Summary – question 6 and TSBC response

Would you consider accepting slightly lower levels of reliability if this resulted in materially lower prices?

TSBC response:

Our members expect that efficiency gains, recent significant network investments and enhanced planning processes, will see reliability of supply improve, without extra cost.

We do not see ourselves being in a position to make a considered judgement as to whether the business value lost as a result of lower levels of reliability would be more than offset by the business value gained from reduced prices.

We note the development at a national level of a regulatory framework to enable that assessment to be made and we propose that the Energy Strategy should incorporate that development.

National framework for distribution reliability

TSBC assumes that question 6 is directed primarily at the reliability of electricity supply, which is subject to extensive regulation, including reliability standards and service level performance incentives.

The Australian Energy Market Commission (AEMC) has developed a framework for setting and regulating distribution reliability in the NEM to promote greater efficiency, transparency, and community consultation in how reliability targets are set. Its final report[34] sets out the recommended framework for distribution reliability in the NEM and the next steps for the implementation of this framework. It also sets out the benefits the framework can deliver, explains how the framework will be applied, and describes the possible different roles played by key participants in the process. Some key milestones in the timeline for developments at a national level are:

- May 2010 - AEMC final report responding to the SCER request on the effectiveness of NEM security and reliability arrangements in light of extreme weather events

- May 2010 – recommendation in the AEMC's final report[35] – that a new requirement be included in the National Electricity Rules for a value of customer reliability, based on the residential consumer class, to be considered when determining the levels for the NEM reliability standard and reliability settings in the wholesale electricity market.

- September 2013 – AEMC final report, framework for distribution reliability, including a recommendation to develop common definitions for expressing distribution reliability targets across the NEM.[36]

- November 2013 – AEMC final report, national framework for transmission reliability;[37]

- March 2014 – AEMO Fact Sheet, value of customer reliability[38]

34 AEMC, FINAL REPORT, Review of the national framework for distribution reliability, 27 September 2013

35 AEMC, FINAL REPORT, Advice to SCER on linking the reliability standard and reliability settings with VCR, 20 December 2013

36 AEMC, FINAL REPORT, Review of the national framework for distribution reliability, 27 September 2013

37 AEMC, FINAL REPORT - Review of the national framework for transmission reliability, 1 November 2013

38 AEMO Fact Sheet, March 2014

- 19 June 2014 – AEMC draft report, distribution reliability measures[39]

The recommended framework includes[40]:

- an economic assessment process to inform setting of reliability targets. This will involve evaluating the way network costs vary with different levels of reliability and explicitly assessing the expected costs of investments against the value that customers place on reliability and the probability of interruptions;
- a transparent and public process for setting reliability targets which requires the assessment and considerations used in setting reliability targets to be published;
- decision making on reliability targets by a body which is independent of the distribution network service providers (DNSPs);
- expressing distribution reliability targets based on the duration and frequency of unplanned interruptions;
- jurisdictional ministers being responsible for determining the appropriate level of reliability with the option to delegate responsibility to the Australian Energy Regulator (AER) or a jurisdictional body;
- the ability for jurisdictional ministers to specify additional reliability requirements for areas of economic or social importance;
- greater opportunities to consult with customers and consider community preferences;
- the use of the Service Target Performance Incentive Scheme (STPIS) to encourage DNSPs to perform to the level of their reliability targets; and
- national reporting and auditing of distribution reliability performance and planning.

The framework provides, at section 11[41,] a comprehensive implementation program, identifying the roles of all relevant stakeholders, including the AEMC, AEMO, AER and state and federal governments and agencies. That program identifies an interim stage, and a four stage implementation of the full program.

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39 AEMC, DRAFT REPORT Distribution Reliability Measures 19 June 2014

40 AEMC, FINAL REPORT, Review of the national framework for distribution reliability, 27 September 2013, executive summary, i

41 AEMC, FINAL REPORT, Review of the national framework for distribution reliability, 27 September 2013, page 89

In parallel with the implementation of the distribution reliability framework the AEMC has developed an implementation plan for a transmission reliability framework, however the distribution reliability framework is more directly related to question 6 posed by the Department. In its November 2013 report the AEMC notes[42]:

"Many of the elements relating to the responsibilities and steps involved in setting the reliability standards for transmission reliability are the same as those recommended for distribution. However our recommended framework for transmission also recognises the inherent different characteristics of transmission and distribution systems. Transmission reliability relates to whether the network is adequate to transport power to demand centres and whether it can withstand various contingencies in a secure manner without serious consequences. Distribution reliability relates to meeting customers' demand while maintaining acceptable levels of quality and continuity of supply".

42AEMC, FINAL REPORT - Review of the national framework for transmission reliability, 1 November 2013, executive summary, iv

42 AEMO Fact Sheet, March 2014

Question 7

Would a review of tariff structures be desirable, in terms of minimizing total network costs?

TSBC response

The TSBC believes that consideration of tariff structures must be accompanied by consideration of the information provided to customers about their electricity consumption, particularly as it relates to the billing process.

Small businesses value any changes which would give them greater control over their electricity consumption and enable reduced costs, and also value changes which reduce the overall cost of producing and delivering electricity, thereby reducing the cost to all customers, and elimination of any existing cross subsidies.

TSBC notes at page 3 of the Energy Strategy Issues Paper – *"Consumers also have responsibilities - to be informed, to make informed choices about energy consumption, and to exercise control over their energy use. What they actually choose to do impacts on efficiency and productivity".*

Most customers (domestic and small business) use and pay for electricity in a manner which does not reflect the value of electricity to their personal lifestyle or their businesses, and the lack of demand-based pricing means that customers are not encouraged to seek to smooth their electricity use, limiting peaks which contribute to higher total costs of delivering electricity to all customers, including small business.

The process by which most small businesses use, monitor and pay for their electricity consumption is basically unchanged from what it was almost 100 years ago. In summary, there is currently no understanding in a real time sense of:

- how much electricity is being consumed;
- the devices and equipment which are contributing to the consumption;
- the price which is being charged;
- the accumulated cost since the last account for payment; and
- the options and opportunities to reduce that cost.

In an era characterised by almost instant communication at a social level (mobile phones, Twitter), and the exponential expansion in the access to and use of information, receiving an electricity bill for consumption three months in arrears is out of place.

The practice of three monthly billing is based on technology and processes which are around 100 years old and blunts any pricing signals which might be sent to customers, limiting their capacity to respond and to reduce their total demand.

In the introduction to this submission TSBC indicated the five fundamental principles which it believes should apply to the Energy Strategy. The current network tariff structure and associated delivery of pricing signals does not comply with those principles.

The past 20 years has seen major changes in the energy sector in Australia and those changes are continuing at a great pace. The overarching objective of those changes is represented in the National Electricity Objective:

> "*The objective of this Law is to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to –*
>
> *(a) price, quality, safety, reliability and security of supply of electricity; and*
>
> *(b) the reliability, safety and security of the national electricity system."43*

Reforms to date have primarily focussed on the supply side of energy delivery, in the case of electricity the generation, transmission, distribution and retailing components within the supply chain. Recent significant electricity price rises have resulted in an even greater focus, particularly on the transmission and distribution components which have been the source of the greatest price rises.

There has however been little real progress on the opportunities to achieve the National Electricity Objective which are available on the demand side – how customers, large and small, use electricity to achieve their personal or business objectives.

A key contributor to the cost of producing and delivering electricity is peak demand. Road infrastructure can be built to a scale less than peak demand (peak traffic volume) with the consequence of increased traffic queues at peak traffic times. Drivers do get to their destinations at peak times but take longer to do so than at off peak times.

In contrast all components of the electricity supply chain must be built to cope with peak demand – there can be no "queues" of electricity. As a result the investment in electricity infrastructure at a national level is estimated at $7.8 billion over the past five years more than it would be if electricity peak demand was smooth, but still the same volume[44].

43 National Electricity Law, section 7.

44 Grattan Institute Fair Pricing for Power, July 2014, p10

Further, the lack of a charge for contributing to peak demand (and thus additional cost) means that those customers who contribute to the peak demand are not paying their share of meeting those costs, resulting in a cross subsidy from other customers to those customers. That situation is contrary to the principles proposed by the TSBC.

Resolution of both those issues (lack of timely information about consumption and price, and lack of demand based pricing) is possible using readily available technology and processes, however most state jurisdictions, including Tasmania, have yet to be convinced of the merits of tackling the issues, including establishing the necessary regulatory arrangements. Similarly, electricity network (distribution) companies have been reluctant to invest in the available technologies without the appropriate political and regulatory environments.

These issues have been debated at considerable length over a number of years and the economic implications of the current pricing, billing and provision of information processes, that is the additional costs imposed on all customers and particularly small business, are well understood.

The Grattan Institutes' Fair Pricing for Power report[45] notes at page 10:

> *"Network tariffs that do not reflect the costs of peak demand can also add to the overall cost of the power system, which means that all consumers have to pay more. Over the past five years, when peak demand was forecast to rise substantially, network businesses invested heavily in new infrastructure. As a result, the regulator allowed them to collect more revenue in the form of electricity price increases. It is estimated that $7.8 billion of network investment over the past five years could have been avoided if customers faced better price signals at peak times".*

The report also notes that domestic customers (households) use 20 to 30 % of total electricity consumed, but use 30 to 50% of electricity consumed at peak times[46]. This implies that addressing the peak demand issue, including appropriate pricing, would deliver lower prices to small and other business customers as those customers (households) contributing the most to peak demand also contribute a greater share to the cost.

The challenge of "winners and losers" as a result of changes to network pricing is addressed in the Fair Pricing for Power report, which suggests[47]:

> *"Governments should anticipate resistance to the proposed changes from customers who benefit from the unfair status quo. Policymakers will need to explain how the proposed changes would make the power system more efficient and cheaper in the*

45 Grattan Institute Fair Pricing for Power, July 2014

46 Ibid, p10

47 Ibid, p19

long run. They should be prepared to stand up for the customers forced to pay cross-subsidies through the existing system".

The Fair Pricing for Power report further notes that this may adversely impact some customers, and proposes "*the need for well targeted concessions to help these households adjust to change."*[48] The TSBC suggests that this would need to be undertaken in accordance with its fourth Principle – "Any variation of prices in order to achieve social equity outcomes is transparent and funding for any resulting subsidies is transparent and equitable".

Application of TSBC's third principle, cost reflective pricing, would address the issues associated with the additional cost of additional network infrastructure required to ensure network stability where there are high levels of solar PV penetration. The resulting additional network costs are currently being borne by all customers who are connected to the distribution network, including small business, thereby delivering a cross subsidy from customers who do not have solar PV generation connected to the electricity network, to those who do.

The TSBC notes that in order to be effective, network tariffs and associated pricing signals must be reflected in full in retail tariffs, which is what customers see, and not bundled or re-shaped in accordance with retailer objectives.

The TSBC also notes the extensive body of work on the broader issue of customer use of electricity undertaken by the Australian Energy market Commission (AEMC) and reported in their Power of Choice review[49].

The final report covers some 289 pages, plus executive summary and recommendations. The recommendations provide a comprehensive overview of the AEMC's view on how to address the issues raised in the TSBC's response and are repeated below for completeness.

The AEMC has received a number of COAG Energy Council (formerly SCER) requests for changes to the National Electricity Rules (NER) and are considering those proposals in line with the statutory consultation process and will be seeking stakeholder submissions and participation.

It is the TSBC's view that the Tasmanian Energy Strategy should recognize and incorporate the work currently in progress at national level concerning network tariffs as part of efficient pricing, flowing from the AEMC's Power of Choice review, and the ongoing work to implement the associated recommendations.

TSBC welcomes the opportunity to contribute to the consultations as part of that implementation process.

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48 Ibid, p19

49 AEMC FINAL REPORT Power of choice review - giving consumers options in the way they use electricity, 30 November 2012

Summary – question 7 and TSBC response

Would a review of tariff structures be desirable, in terms of minimizing total network costs?

TSBC response:

Yes. Changing network tariff structures, with the resulting tariffs reflected in retail tariffs, will, over time, deliver lower electricity prices to all customers and will eliminate existing cross subsidies which do not favour small business.

Changes to network tariffs are part of a larger issue, being consumer engagement in managing their electricity consumption, and must be accompanied by changes in the way in which information about consumption and prices is provided to electricity customers.

We note the development at a national level of a series of actions to progress such changes and we propose that the Energy Strategy should incorporate that development.

AEMC FINAL REPORT - Power of choice review - giving consumers options in the way they use electricity

List of final recommendations for the review

Consumer awareness, education and engagement (Chapter 2)

1. A comprehensive communication/education strategy is developed to support implementation of the reforms recommended in this review, and to more broadly improve consumer understanding of energy use and relationship to costs. A SCER working group should be established (with participation of stakeholders from consumer organisations and the electricity sector) to develop and manage application of the strategy. This would be supported by the proposed principles in the report for undertaking consumer engagement.

2. There is a review of government energy related education and information programs (ie energy efficiency schemes) to ensure an effective and appropriate focus on specific consumer segments.

3. There is a review of the existing retailer switching arrangements to better support consumer choice and to make switching retailers more efficient. The review should assess whether a maximum day limit could be introduced in the NEM.

4. The National Energy Customer Framework is amended to include a framework which governs third parties (non-retailers and non- regulated network services) providing energy services to residential and small business consumers. The framework would outline which aspects of the National Energy Retail Rules (NERR) apply, and in what circumstances. AER guidelines would be developed to outline NECF exemptions for these services.

Consumer information – access to electricity data (Chapter 3)

5. The NER is amended to clarify the arrangements and provide a framework for consumers to request and receive their energy and metering data from their retailer. The framework would provide for: — minimum format and standard information that would need to be provided to consumers;

— timeframes for delivery of data (ie no costs for standard data format once a year);

— fees that can be charged when consumers request their energy and metering data;

— ability for a consumers agent to access energy and metering data directly from the consumer's retailer (this would be in accordance with appropriate explicit informed consent arrangements); and

6. Amendments are made to the NERR to provide each residential and small business consumer with their consumption load profile. At a minimum this should be on a consumer's retail bill.

Enabling technology (metering) (Chapter 4)

7. A new framework is introduced in the NER that provides for competition in metering and data services for residential and small business consumers. The SCER endorsed minimum functionality specification for smart meters would be required for all future metering installations.

8. A framework for open access, interoperability and common communication standards is established to support competition in DSP energy management services enabled by smart meters.

9. The NER require that smart meters be installed in defined situations (ie new connections, refurbishments and replacements). These would also be as per the minimum functionality specification.

10. The option of a government mandated roll out of smart meters in the National Electricity Law is removed. This will provide certainty to the market to proceed with commercial investment.

Demand side participation in wholesale electricity and ancillary services markets (Chapter 5)

11. A demand response mechanism is introduced that pays demand resources via the wholesale electricity market (rewards changes in demand). Under this mechanism demand resources would be treated in a manner analogous to generation and be paid the wholesale electricity spot price for reducing demand. We recommend that AEMO develops the details for a rule change proposal and required procedures, including the baseline consumption methodology.

12. The NER is clarified regarding AEMO's role in demand forecasting for its market operational functions.

13. A new category of market participant for non-energy services is introduced in the NER to unbundle the sale and supply of electricity from non-energy services, such as ancillary services.

Efficient and flexible pricing (Chapter 6)

14. There is a gradual phase in of efficient and flexible retail pricing options for residential and small business consumers through the introduction of cost reflective electricity distribution network pricing structures. The phase in of cost reflective network pricing would be through segmenting these consumers into three different consumption bands and applying flexible, (ie time varying) retail pricing options in different ways as outlined in the final report.

15. To complement the gradual phase in of efficient and flexible retail pricing options and support those consumers with limited capacity to respond, governments review their energy concession schemes and target government energy efficiency programs.

16. Amend the NER distribution pricing principles to provide better guidance for setting efficient and flexible network price structures that support DSP. This includes improving the existing consultation requirements to ensure that consumer impacts are taken into account in price structures/design.

17. Amend the NER to require that a residential and small business consumer's consumption (where they have a meter with interval read capability) is settled in the wholesale market using the interval data and not the net system load profile. This will be the case irrespective of the consumers' retail tariff structure.

Distribution networks and DSP (Chapter 7)

18. Reform the application of the current demand management and embedded generation connection incentive scheme in the NER to provide an appropriate return for DSP projects which deliver a net cost saving to consumers. This includes creating separate provisions for an innovation allowance.

19. Adopt a two-part approach to address the issue of business profits being dependent upon actual volumes. Firstly, improvements to the pricing principles to guide network tariff structures and secondly, include allowance for foregone profit under the revised demand management incentive scheme.

20. Make minor amendments to the NER to provide (a) clarity that AER can have regard to non-network market benefits when assessing efficiency of expenditure; and (b) flexibility in annual tariff process to manage potential extra volatility of DSP costs.

Distribution Generation (Chapter 8)

21. The AER should give consideration to the benefits of allowing distribution businesses to own and operate distributed generation assets when developing the national ring fencing guidelines for these businesses.

22. As part of the review into a national approach to feed in tariffs, consideration be given to the ability of time varying tariffs to encourage owners of distributed generation assets to maximise export of power during peak demand periods.

Energy efficiency measures that impact or seek to integrate with the NEM.
23. There needs to be greater coordination of energy efficiency regulatory schemes and DSP options available. The objective is to achieve greater recognition of the value for peak demand reductions and the changes to the load profile from the existing energy efficiency schemes.

24. Improve reporting and availability of publicly accessible data on the load shape impacts of energy efficiency measures on both peak and average electricity demand.

Question 8

What approach, including non-regulatory ones, should Government consider for improving the thermal efficiency of our buildings?

TSBC response

In accordance with TSBC's Principle 2 described in the introduction to this submission, any proposal to reduce total energy consumption and reduce energy costs in the long term, thereby reducing costs to small business, is endorsed in principle by the TSBC, subject to the qualification that associated compliance or other costs imposed on small business do not exceed the reduced energy costs and other benefits.

The TSBC contends that for any scheme aimed at improving the thermal efficiency of all building stocks (our buildings) to be successful, there must be an appropriate balance between environmental and economic objectives. Where the scheme involves compliance obligations which are difficult and/or costly to meet the scheme may not secure the necessary stakeholder support to be implemented, or might lose support after implementation. Alternatively where the compliance obligations were set too low there would be little incentive to develop the means, technological and other, to meet the obligations. Any capital costs involved in achieving a greater thermal efficiency would also be part of the associated cost-benefit analysis.

Clear financial benefits can be derived from buildings, both residential and commercial, with low energy consumption, including premium rents, reduced operating costs and reduced maintenance costs. Additionally, reduced energy consumption in buildings will contribute to a reduction in total energy consumption, reduce the need for further investment in energy infrastructure and therefore reduce future energy costs.

TSBC notes the application of the Building Code of Australia in delivering greater thermal efficiency, and also the application of the Building Energy Efficiency Disclosure Act 2010.

The TSBC also notes that the scale of the improvement in thermal efficiency of buildings and the associated benefits has the potential to be large. Renovate Europe is a political communications campaign with the ambition to reduce the energy demand of the EU building stock by 80% by 2050 compared to 2005 levels through legislation and ambitious renovation programmes[50]. At the launch of the Commercial Building Disclosure program on 1 November 2010 the (then) Parliamentary Secretary for Climate Change and Energy Efficiency indicated "… *commercial buildings currently account for about 10 per cent of Australia's total greenhouse gas emissions. Improving the energy efficiency of buildings is one of the fastest and most cost-effective ways to reduce Australia's carbon emissions,"*[51]

50 The Renovate Europe campaign was initiated by EuroACE in 2011. http://www.renovate-europe.eu

51 Department of Climate Change and Energy Efficiency: 1 November 2010, press release

Schemes to improve the thermal efficiency of building stocks exist in Australia, for example the BASIX scheme in NSW[52], and abound around the globe.

The TSBC proposes that improving the thermal efficiency of buildings is a worthy objective, and inclusion in the Energy Strategy is appropriate, subject to the caveats discussed later in this section.

TSBC proposes that such a scheme should be multi-dimensional, including:

- Political will.
  Improving the energy efficiency of buildings would need to be integrated into a number of policy areas. Step change improvement will not happen without strong commitment and guidance at Government level.

- Mandatory targets.
  Real outcomes where political policy objectives require behaviour change are rarely delivered without mandatory targets. Such targets might include, for example, a conversion rate for existing building stocks.

- Identification of energy efficiency ratings.
  Applicable to both domestic and commercial buildings, mandating the identification of the energy efficiency ratings of buildings which are sold or leased provides information to potential buyers or tenants. It could be expected that energy efficient buildings would attract premium prices, which would pass through to conversion rates.

- Financial support.
  Building owners can be expected to respond favourably where the benefits of constructing or converting buildings in accordance with new thermal efficiency standards deliver favourable financial cost benefit outcomes. There may however be impediments such as the need to raise the necessary capital for conversion, which could reduce the take up of conversions. As part of any proposed scheme it may be appropriate for the state to provide funding at concessional rates, where the cost of that concession is exceeded by the benefits to the broader community.

- Enforcement mechanisms.
  Appropriate enforcement mechanisms, through legislation and regulations, including sanctions, would be necessary to provide maximum assurance that mandatory targets would be met.

- Communication, motivation and education.
  TSBC's observation is that building owners remain largely unaware of the potential economic benefits of improving energy efficiency. Imaginative communication

52 www.basix.nsw.gov.au/

strategies are needed to stimulate awareness, motivate and inform. Improving the energy efficiency of buildings should be seen as a desirable and responsible thing to do.

The TSBC's endorsement of any such scheme would be subject to demonstrable net cost benefits flowing to small business over the long term, with no increase in costs in the short term.

TSBC also proposes that any such scheme should not impinge unduly on normal commercial decision making. Small businesses are often heavily capital constrained and acquiring the long term benefits of improved thermal efficiency in buildings they own may not be achievable if the initial costs are too high. The targets and compliance regime of any scheme to improve the thermal efficiency of buildings needs to recognize and cater for that reality.

Summary – question 8 and TSBC response

What approach, including non-regulatory ones, should Government consider for improving the therm*al efficiency of our buildings?*

TSBC response:

TSBC endorses in principle any proposal to reduce total energy consumption, reduce energy costs in the long term, and therefore reduce costs to small business.

Subject to the qualification that associated compliance or other costs imposed on small business do not exceed the demonstrable reduced energy costs and other benefits.

TSBC has proposed the structure of a five element scheme to deliver improvements in the thermal efficiency of Tasmania's building stocks and would be happy to discuss this with the Department or Energy Working Group.

Question 9

What approach to energy efficiency should Government use to help improve productivity for small to medium businesses, and to reduce energy bills for households?

TSBC response

The TSBC notes that the Issues Paper (p20) identifies that there are many different program approaches aimed at stimulating the uptake of energy efficiency measures, and notes the National Strategy on Energy Efficiency[53] and Tasmania's response, including its Future Directions (energy efficiency) proposals[54]. The TSBC has nonetheless examined a large number of the programs adopted nationally and internationally and considers the Productivity Commission's "The Private Cost Effectiveness of Improving Energy Efficiency"[55] provides the most useful guidance. Key points from that report (paraphrased) are as follows[56]:

- Firms and households generally do not deliberately waste energy but energy has been cheap and is only a small percentage of total outlays therefore energy efficiency has not been a high priority;
- The most important barriers to the adoption of privately cost-effective energy efficiency improvements appear to be:
    - a failure in the provision of information; and
    - the different incentives facing those who take decisions about installing energy-efficient products and those who might benefit from using them.
- Some government intervention to address these problems is appropriate. The Commission favours light-handed regulatory responses and information provision rather than more prescriptive and intrusive approaches; and
- Some energy efficiency measures may not be privately cost effective, and yet may generate net public benefits because of their environmental outcomes. Those measures may prove to be sound public policy, but they should be considered against other means of achieving those environmental objectives.

The TSBC notes the Issues Paper focus on energy efficiency for households and small to medium businesses and endorses that approach, on the basis that large businesses' focus on energy costs, because of the scale of those costs, is generally more informed and targeted at minimisation than most households and small to medium businesses.

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53 Council of Australian Governments (COAG), National Strategy on Energy Efficiency, Updated July 2010

54 Department of Premier and Cabinet website, Saving energy costs in homes and businesses.

55 Productivity Commission Inquiry Report, The Private Cost Effectiveness of Improving Energy Efficiency August 2005

56 Ibid, pxx

The TSBC does not support the mandatory imposition of any energy efficiency scheme involving a direct additional cost to domestic and business customers, including those which result in increased retail energy prices, on the basis that invariably the additional costs borne by energy customers, including reporting and compliance costs, outweigh any demonstrable benefits.

Instead the TSBC proposes that the Government's approach to improving energy efficiency for households and small to medium businesses should be multi-faceted and incorporate the following elements:

- Competition in the retail electricity market, combined with a market framework which facilitates new market participants offering competitive services such as load management and energy efficiency.

- *Information access*. The TSBC notes the difficulties encountered when internet searching for energy efficiency opportunities in Tasmania, without knowing first the name of the scheme or relevant service provider. Information on energy efficiency improvement opportunities for households and small to medium businesses should be made available via a readily accessible, easy to find Government sponsored website, (for example – Victoria's "Switch On" site - http://www.switchon.vic.gov.au/) with links to other websites for businesses which provide energy efficiency services, such as Energy Conservation (http://www.energyconservation.com.au/). A cost effective customer awareness campaign should be established to provide regular "pointers" to the website.

- *Information access*. Aurora Energy should update its website front page and list energy saving opportunities as one of the key headings (currently, carbon tax, manage your bill and Aurora PAYG are the key headings, with energy saving tips located under the "manage your bill" banner), and provide a highly visible link to the Government's energy efficiency website.

- *Energy efficient appliances and buildings*. Related to our response at question 8, the Government should adopt the latest standards on energy efficiency applicable to appliances and to building codes, domestic and commercial.

- *Price differentiation*. The Government should examine all opportunities within its remit to deliver price differentiation whereby energy efficient options in any product or service are cheaper than an alternative relatively inefficient option. An existing example is the registration cost of a vehicle powered by a small engine compared to one powered by a larger engine, which could be translated to (for example) land tax assessments including a component based on the energy efficiency of any buildings in the assessments.

- *Price differentiation*. As discussed in our response to question 7 the current tariff structure should be revised to encourage demand side participation by electricity consumers, targeting reduced total demand and reduced peak demand. The revision of tariff structures should be accompanied by a modernisation of the processes and technologies by which energy consumers are made aware of their consumption and the cost.

- *Utilisation of electricity – commercial electricity customers*. Commercial customers' connection agreements with electricity network companies, where demand exceeds a nominated total, include a requirement that the customer's power factor will not be lower than a prescribed percentage. Power Factor is a measure of how effectively incoming electricity is used in electrical equipment, particularly motors, transformers and high intensity discharge lighting, and is expressed as a number between 0.0 and 1.0.

  A power factor of 0.7 means that only 70% of the electricity consumed is actually being used productively, resulting in increased demand, total and peak, and higher costs, for the customers directly concerned and across the electricity supply chain, therefore all customers.

  Electricity network companies (in Tasmania, TasNetworks) specify power factor requirements, but do not have the means to measure it. The Government should consider mandating power factor audits for businesses with electricity demand (total and peak) above specified levels.

- *Direct funding*. The Issues Paper identifies a number energy efficiency programs funded by the Government, such as Stay Warm, save Money. The TSBC is of the view that such programs have merit, subject to a number of caveats:

  - The programs should form part of an overall strategy, with measurable, time based targets for energy efficiency outcomes (such as conversion rate of building stocks, energy reductions achieved for nominated target customers).
  - Fully costed program elements, with detailed implementation timelines.
  - Fully costed expected benefits, where expected benefits are greater than implementation costs and any indirect costs flowing to other electricity customers.
  - Mechanisms to identify and public report results achieved.
  - Nominated check points at which program elements are ceased if expected progress is not achieved.

- *Smartgrid.* The new technologies and processes which are currently available to electricity network companies to inform and enable customers, as mentioned in our response to question 7, have the added potential benefit of enabling network operators, or other market participants, to manage the electricity delivered to homes and businesses in such a way that peak demand can be reduced, by remote operation of devices on the network and within homes and businesses, to achieve that reduction. There area range of market options for determining who controls the electricity load and how the costs and benefits are shared amongst market participants. The potential benefits are large and the TSBC recommends that the Government consider the potential benefits as part of its review of pricing and communication options, on the basis that services are provided via a competitive market framework.

Summary – question 9 and TSBC response

What approach to energy efficiency should Government use to help improve productivity for small to medium businesses, and to reduce energy bills for households?

TSBC response:

TSBC notes the work already in progress via the National Strategy on Energy Efficiency and Tasmania's response, including its Future Directions (energy efficiency) proposals.

TSBC proposes that the government should implement an energy efficiency program which is multi-dimensional, including information access, price differentiation, power factor improvement, direct funding and smartgrid development.

Directly funded sub-programs should only be implemented where demonstrable benefits outweigh implementation and other costs.

TSBC does not support the mandatory imposition of any energy efficiency scheme involving direct or indirect additional cost to domestic and business customers,

Question 10

What role should Government play in attempting to retain and increase load growth in Tasmania and how should it do it?

TSBC response

Question 10 is posed against a background of falling electricity demand, across the National Electricity Market (NEM) and in Tasmania, creating a generation surplus, which is projected to lead to lower wholesale prices.

The TSBC refers to its previous advices, in this and other submissions, suggesting that the Government should focus on establishing competitive wholesale electricity and retail markets in order to lower electricity prices and thereby support business growth across all sectors of the Tasmanian economy, not just large, energy intensive business.

The TSBC believes that by facilitating that outcome, efficiently operated electricity businesses will deliver competitive prices which will in itself assist to attract business growth, as opposed to any government intervention.

The TSBC is also strongly of the view that market forces should be allowed to prevail to address the current oversupply, as is the case across the National Electricity Market at present, where the highest cost generation plants are being retired or mothballed, particularly in Queensland and NSW.

The TSBC has previously commented[57] on the Government's methodology for determining regulated wholesale electricity prices, in the absence of a competitive market. That methodology, as noted by the TSBC[58], is well considered and imposes appropriate obligations on Hydro Tasmania. The TSBC remains firmly of the view however that regulation is a second best option:

> *"It is exceptionally difficult to design a regulatory regime that is a good substitute for a market (eg. having to deal with information constraints and inflexibility in responding to changing circumstances)."*[59]

The TSBC notes the reference in the Issues Paper, introduction to question 10, p22-

57 TSBC – Response to the Tasmanian energy Regulator's Position Paper, Market and Regulatory Framework, March 2013

58 Ibid, p29

59 Ibid, p39

> *"As the owner of three key companies in the electricity supply chain the Tasmanian Government may have the capacity to use energy pricing to differentiate itself from other jurisdictions (both within Australia and abroad) and potentially attract new industries and, consequently, load growth."*

The TSBC is strongly of the view that the function of establishing the regulated wholesale and retail prices should be solely the domain of the Tasmanian Economic Regulator (TER), independent of government, to ensure the integrity of electricity markets and to ensure that market participants can have confidence in the outcomes of the independent processes.

The Independent Expert Panel recommended as follows:

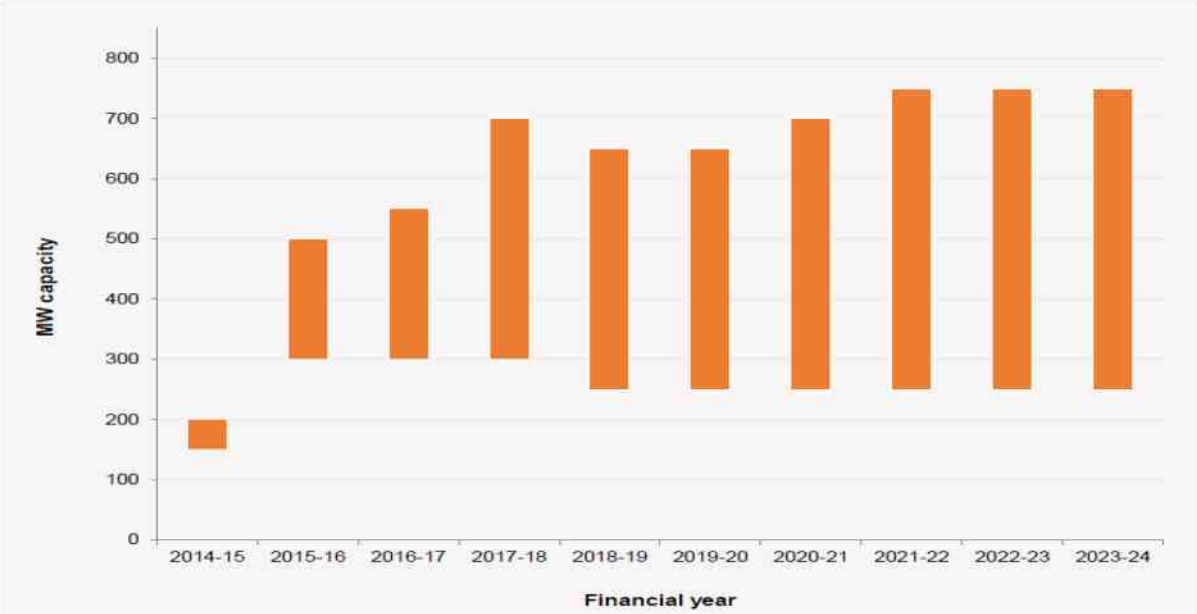
> *"6. The TER is given the discretion to independently apply appropriate approaches and methodologies, within the context of principles and objectives set by the regulatory framework. If there are specific outcomes that the Government considers should be taken into account, then it may put the case to the TER in submissions to the independent regulatory process".*[60]

The TSBC is of the view that, allowed to function as designed, the current methodology applied by the TER for establishing regulated wholesale prices will respond to prevailing conditions across the National Electricity Market (NEM), being a current and projected over supply of electricity. Similarly the methodology for setting retail prices applied by the TER will translate that wholesale price response into retail prices.

In its latest electricity Statement of Opportunity, analysis by the Australian Energy Market Operator (AEMO) indicates that Tasmania will have an electricity surplus, under any of its projected low, medium and high demand growth scenarios, beyond 2023/24, as shown in figure 3 below.

60 An Independent Review of the Tasmanian Electricity Supply Industry, Final report, March 2012

Figure 5 Surplus capacity (generation) Tasmania



Source – AEMO, Electricity Statement of Opportunities for the National Electricity Market, August 2014.

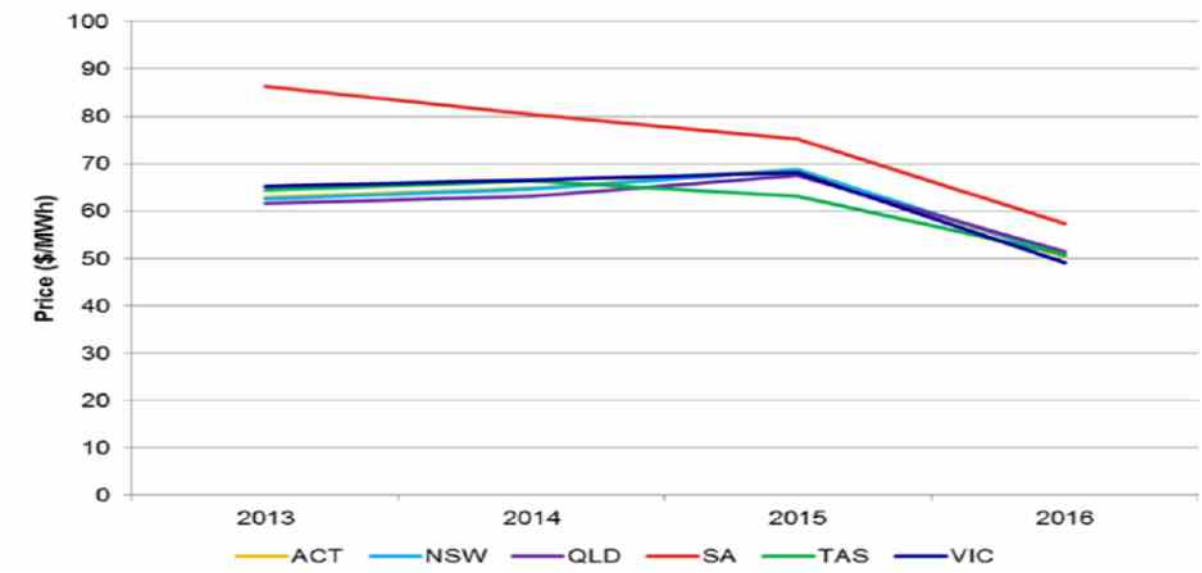
The actual and projected fall in demand is driven by a combination of factors, including consumer response to electricity price increases; energy efficiency gains; the take-up of solar photo voltaic generation; increased use of gas as an alternative fuel and the effects of the global financial crisis flowing through to consumer demand and business performance.

In any competitive market, particularly those without distortions as a result of interventions such as those designed to achieve greenhouse gas reductions, over supply will result in lower prices and if the oversupply is sufficiently large some high cost producers will exit the market.

In its 2013 review of wholesale electricity prices in the NEM, [61] NERA Economic Consulting projected that wholesale electricity purchase costs (spot price plus hedge costs) would fall, as shown in figure 4 below. The projections do not take account of the abolition of the carbon tax, or any effect of possible changes to the Renewable Energy Target scheme(s), which would result in projected purchase costs falling further.

61 Wholesale Electricity Costs in the NEM A Report for the Australian Energy Market Commission Advice on Best Practice Retail Price Regulation 19 August 2013

Figure 6 Projected wholesale electricity purchase costs, by NEM region



Source – NERA Economic Consulting, report for AEMC, 19 August 2013.

NERA predicts that Tasmanian wholesale prices will fall and, as noted above, the process administered by the TER will translate that fall into retail prices.

The TSBC contends that should the Government wish to vary the wholesale or retail prices determined by the TER's independent process, such as to deliver a lower price outcome to all or some customers, or to protect its revenue streams delivered by state owned electricity businesses (SOEBs) then it should do so via the established regulatory process or by way of alternative, transparent funding arrangements.

The TSBC notes the use of new entrant peaking plant as part of the calculation of load following swap prices in the Wholesale Contract Regulatory Instrument[62]. We believe the use of new entrant pricing in an environment of over supply could inflate wholesale prices above what would be the case in a competitive market situation. The TSBC suggests that a revised methodology be implemented, based on an average of the long run marginal cost of lowest cost generation plant which meets the current load.

On the matter of seeking to increase load growth, the TSBC notes that aiming to achieve increased energy efficiency (Issues Paper question 9) and therefore reduced demand (load), at the same time as aiming to increase energy demand (load growth) appears on the surface to be somewhat counter intuitive.

62 Refer Treasury and Finance - Regulation of Hydro Tasmania's wholesale electricity contracts in Tasmania, Framework Guide, August 2013, p5

The TSBC acknowledges however that the focus on energy efficiency to date has been driven primarily by a focus on climate change, and the need to reduce carbon emissions. Reducing the need for new electricity infrastructure (generation and network) has also been an important focus, with the objective of avoiding or deferring future capital expenditure.

From the time that demand for electricity started to fall and medium to long term projections (such as AEMO's 10 year forecasts) began predicting electricity generation surpluses for the foreseeable future, the implications of reduced and reducing demand for the utilisation rates and assets values has prompted a re-evaluation by the owners of existing electricity infrastructure, with the emphasis shifting to asset utilisation and forward projections of capital expenditure.

The nature of the regulatory process for determining network (transmission and distribution) prices means that unit network prices would increase as a result of reduced demand, that is, each existing customer, large or small, will pay a greater amount as their share of the total revenues of the transmission and distribution businesses (now TasNetworks) in the absence of asset value write downs.

The regulatory process administered by the Australian Energy Regulator should however deliver the same outcome as a competitive market in an oversupply situation, that is reduced prices, primarily via a reduction in asset values, corresponding to the exit of producers in a competitive market.

Given the electricity supply surpluses projected by AEMO, government ownership of assets in each component of the electricity supply chain in Tasmania means that the state's revenues and net asset values will potentially also fall, as will the net wealth of all Tasmanians. The unique nature of Hydro Tasmania's generation capacity means there need be no exit of generators from the market, with the possible exception of the Tamar Valley power station, however generation and network assets will be underutilised, a situation which would be considerably worsened in the event of the departure of an existing Major Industrial (MI) customer.

The TSBC therefore believes that new electricity customers should be attracted by lower prices which arise as a result of market forces, or a regulatory process which mimics market outcomes, not by intervention, and by the competitive advantages Tasmania has to offer beyond electricity prices.

The TSBC notes however that every state and Territory in Australia can be expected to be seeking to attract new business for the same reason as Tasmania, therefore it should expect fierce competition for that business. As noted in the Issues Paper, this will be a key role for the Department of State Growth. Tasmania's geographic isolation (Bass Strait) would most likely limit the number of energy intensive industries which have the most potential for development in Tasmania, essentially to those industries which would not require raw

materials to be imported. The availability "on island" of abundant, low cost resources (copper, zinc, iron) matched with very low cost electricity which drove "hydro industrialisation" is not a scenario which presents itself in 2014.

Downstream processing of forest products, via a pulping process, is energy intensive, however a pulp mill would produce enough electricity for its own operations, (80MW) plus electricity to sell into the grid (100MW)[63], and would therefore add to the current over supply situation.

The TSBC believes Tasmania does have natural advantages which the Department of State Growth should be able promote in its efforts to attract new industry, including:

- A safe, secure location far from major volatile and unstable regions in the world particularly war affected areas;
- The close proximity of a major airport;
- Relatively low cost land and accommodation, both industrial and domestic;
- Electricity network infrastructure in Hobart, Launceston, Devonport and Burnie which is robust and recently upgraded;
- Potentially – communications advantages using existing fibre optic assets owned by the state owned electricity businesses, in addition to NBN assets; and
- Electricity from renewable sources.

Such advantages should be promoted to attract customers such as IT technology or data centres, the banking industry and internet service providers who value those attributes.

63 Gunns Ltd. Fact Sheets – Bell Bay Pulp Mill, October 2011.

Summary – question 10 and TSBC response

What role should Government play in attempting to retain and increase load growth in Tasmania and how should it do it?

TSBC response:

TSBC does not support Government intervention in the setting of wholesale or retail electricity prices for domestic and commercial customers in order to stimulate load growth, or to support the financial position of the state owned electricity businesses.

Competitive wholesale and retail markets are the TSBC's preferred options for price setting, which would over time deliver reduced electricity prices to small business and other electricity users.

In the absence of competitive markets the recently revised regulatory processes, administered by the Tasmanian Energy Regulator, must remain independent of Government.

Tasmania does have a range of competitive advantages which should be promoted by the Department of State Growth in its efforts to attract new business.

Question 11

What further potential is there to develop renewable energy in Tasmania, including wind energy, given there is no unmet Tasmanian demand requiring additional generation for the foreseeable future?

TSBC response

The TSBC believes that the development of any extra generation capacity, including renewable, should be supported by a sound business case. In the present oversupplied electricity market such an investment is not required to meet local demand for the foreseeable future and if the electricity produced were exported it would be delivered to an already oversupplied market, with declining prices. If the Government or a state owned electricity business were to be the investor in any additional renewable energy, any shortcomings in the business case could be expected to add to electricity costs, or to impact adversely on government services or require additional revenue (tax) measures, none of which would be welcomed by small business.

Projected domestic and small/medium business demand will not require new generation for the foreseeable future and the only scenarios that would are the entry of a new, energy intensive customer, or a prolonged period of lower than average rainfall, worse than Tasmania has experienced to date.

The TSBC suggests that private investment in renewable energy generation may occur, where such an investment results in reduced overall business costs in the case of co-generation or embedded generation; or where the investment is in a low cost renewable energy process (not yet identified) whereby the energy produced could be sold at a profit to the oversupplied market. In either case the energy produced would add to the current oversupply situation. Small business is attentive to the relative cost of alternative energy sources and notes the continuing reduction in the cost of solar energy (without considering concessional feed in tariffs) as both gas and electricity prices from conventional sources continue to rise. It could be that, at a point in the medium term, solar PV and battery technology will present a cost effective alternative to conventionally delivered energy for some small businesses.

In the meantime the payment of prices above avoided generation cost for renewable energy produced from solar photovoltaic generation, domestic or industrial scale, is and will continue to contribute to the existing oversupply.

The TSBC considers that whether or not there is potential for further development of renewable energy in Tasmania by the Government or by state owned electricity businesses depends on the expectation of a future scenario which would result in such development adding value to the Tasmanian economy over the long term.

The TSBC is strongly of the view that a full analysis of a range of credible future scenarios including the potential loss of one or more major industrial customer, as part of the development of an Energy Strategy, is essential to ensure that any policy decision regarding investment in energy assets, along with changes to market structures or regulation, is taken against the fullest possible information set.

The TSBC notes that in the mid 1990s there were two schools of thought concerning the next source of generation – one proposing Basslink and one proposing bringing natural gas ashore as an alternative energy source to electricity, with the potential to be used in electricity generation. The ramifications of both options progressing, and how they might be optimised, were not fully analysed (in a form available to the public) before the commitments to each were concluded, which contributed to the current over-supply of electricity and the looming under-utilisation of the gas transmission pipeline.

The TSBC sees that outcome as a consequence of policy makers being wedded to a particular action, without reference to a broad and well considered, well analysed strategy, and suggests that such an outcome should not be repeated. The development of the Energy Strategy has the potential to avoid a re-occurrence.

It is therefore of some concern that the Government's "Looking to the future with energy"[64] document indicates that *"The Liberals will commit $2.5 million of funding to advance the case for a second interconnector, and the case for the expansion of Hydro Tasmania's generation output by 10 per cent."*[65] This would appear to have the elements of putting a desired action ahead of a well-developed argument as to why such an action should proceed, and why the action is the best option to achieve the desired strategic outcomes. The TSBC notes the NEM wide generation surplus, the recent abolition of the carbon tax and the current review of the Renewable Energy Target scheme(s) and is concerned to ensure that no additional cost burden is imposed on small business as a result of poor investment decisions by the Government or any market participant.

The TSBC suggests that the $2.5M funding might be better invested in developing the Energy Strategy, including undertaking scenario analysis which will be required to ensure the Strategy delivers the greatest possible value. Whether or not an increase in hydro generation capacity or a second interconnector best achieves the objectives identified in the Strategy would be revealed in the scenario analysis. If so, the resulting investment would then be expected to be the subject of business case consideration.

64 Looking to the future with energy, ww.tas.liberal.org

65 Ibid, p3

The TSBC wishes to propose what the contents of a well-developed Energy Strategy might include, and notes that there are numerous examples from which to draw guidance. Two such examples include Queensland's 30 year electricity strategy[66], (in development) and New Zealand's Energy strategy to 2050[67].

In proposing the contents the TSBC notes the terms of reference for the Independent Review[68]:

> *The Expert Panel shall investigate and report on:*
>
> *"7. Actions that would guide and inform the development of a Tasmanian Energy Strategy particularly in relation to the Government's primary objectives of minimising the impact on the cost of living in Tasmania and ensuring Tasmania's long term energy sustainability and security".*

The TSBC recommends that the findings and recommendations of the Expert Panel and its proposed action plan[69] should form the basis of the Energy Strategy section - immediate challenges and actions.

The contents of energy strategy should include (but not be limited to):

- A clear vision statement and objectives against which any proposed actions can be tested;
- The vision statement would articulate, among other things, the Governments "green appetite", and the extent to which environmental outcomes should be balanced against cost;
- Two sections – immediate/short term (1 to 5 years) and long term (6 to 20 years);
- The challenges and opportunities in each section (1 to 5 years, 6 to 20 years);
- Actions and responses to the immediate/short term challenges and opportunities (note - recommendations of the Independent Review)[70] which must align with long term strategies;
- A range of future (6 to 20 years) credible scenarios of supply and demand;

66 The 30-year electricity strategy, Discussion paper, Powering Queensland's future, 2013

67 New Zealand energy strategy to 2050, Powering Our Future, October 2007

68 An Independent Review of the Tasmanian Electricity Supply Industry, Final report, March 2012, p iii

69 Independent Review of the Tasmanian Electricity Supply Industry, final report, March 2012

70 Ibid, Appendix 7

- Analysis of lowest cost options to meet any projected supply shortfall and to optimise any supply surplus;
- The projected mix of electricity generation, including replacement of existing plant, and the impact of local generation, in particular solar PV, rooftop and industrial;
- The role of private investment;
- An assessment of hydrological risk and the most cost effective means of mitigating that risk;
- The results of economic modelling of each scenario against a range of parameters, including electricity prices, financial inflows and outflows to the State, and social equity outcomes;
- The most economically efficient mix of electricity and gas to meet domestic and small business energy needs;
- The role of technology – smartgrid; and
- Actions proposed to address long term challenges and opportunities, based on the assessment of the most likely scenario.

Summary – question 11 and TSBC response

What further potential is there to develop renewable energy in Tasmania, including wind energy, given there is no unmet Tasmanian demand requiring additional generation for the foreseeable future?

TSBC response:

Private investment in renewable energy, business case driven, will occur regardless of the current over supply situation, and can be expected to be mostly small scale, embedded generation. The payment of prices above avoided generation to solar photovoltaic generators is and will continue to contribute to the existing oversupply. Low cost solar energy is an emerging reality.

Any development of renewable energy by the Government or by state owned electricity businesses should be guided by the Energy Strategy and be subject to business case evaluation.

TSBC has proposed a broad outline of the contents of the Energy Strategy, which would include section one covering immediate challenges and actions and section two covering a description and evaluation of long term credible scenarios and actions associated with the most likely scenario.

TSBC recommends that the findings and recommendations of the Expert Panel's Independent Review should form the basis of the immediate challenges and actions section of the Energy Strategy.

Question 12

Is there a further facilitation role for Government in gas roll-out, or should Government focus its efforts on examining the costs and benefits of improving minimum protections for gas customers?

TSBC response

The (then) government's 2003 investment in the gas distribution system, operated by Tas Gas Networks (formerly Powerco), was around $55 million, or around $5,000 per connection of each currently connected customer (around 12,000 in total).

The decision to bring natural gas to mainland Tasmania was in accordance with the 1997 Directions Statement's[71] objectives, progressed by successive Tasmanian governments:

1. Securing new sources of supply to meet load growth;
2. Mitigating the State's exposure to hydrological risk; and
3. Introducing greater competition and customer choice into the Tasmanian energy and electricity market.

As noted in the Issues Paper[72], gas was envisaged as a product of choice and is delivered to domestic and commercial customers via privately owned transmission and distribution entities, and a mix of private and government owned (Aurora Energy) retailers, with no retail price regulation.

Natural gas is an energy option which competes with electricity, wood (heating) and with liquefied natural gas (for domestic and small business customers – bottled gas), and since 2003 has provided a price competitive energy alternative.

The price competitiveness of natural gas has however changed rapidly for the worst in the recent past and is set to worsen even further in future years.

The two drivers for that situation are the squeeze on locally available natural gas on Australia's eastern seaboard (from where Tasmania's natural gas supply is drawn) resulting from the attractiveness to gas producers of the export market, and the cessation of take or pay obligations currently in place on the gas transmission pipeline between Victoria (Longford) and Tasmania (Georgetown) in 2017, coupled with the declining utilisation of the gas fired Tamar Valley power station.

71 10 April 1997 speech to the Tasmanian Parliament, Honourable Tony Rundle

72 Energy Strategy Issues Paper, Department of State Growth, p12

Total annual gas demand nationally is expected to increase from 745PJ in 2014 to 2,182PJ in 2033, with the projected supply shortfall (where no further infrastructure development occurs) growing from 2015 to around 250PJ in 2033.[73]

The combination of increased demand and projected possible production shortages in the wholesale gas market and reduced utilisation of the gas transmission pipeline to Tasmania is a very large double whammy, which *"has the potential to see delivered natural gas prices increase 300% in five to ten years"*[74].

Goanna Energy reported in July 2014 that *"small business and residential pricing increasing by 6%, but large industrial users are experiencing severe price increases of up to 35%, with little positive news in sight"* [75].

Analysis by Goanna Energy, as detailed in figure 5 below, suggests a rise in delivered gas prices over the next three years of around 200%.

Figure 7 Gas price drivers 2014 to 2017

• Gas energy	100% - 220% *
• Transmission	103% - 238% **
• Retail	100% - 150% ***
• Network	26% - 100% ****

* Price predictions range between $9.00 and $16.00 per GJ
** Palisade response to Market and Regulatory Framework Position Paper, March 2013
*** Retail margin maintained at current level
**** Network charges negotiated by individual industrial customers

Source – Goanna Energy Consulting, presentation to the TCCI, March 2014

It is therefore highly unlikely that any further investment in gas infrastructure would deliver a positive return, as the delivered product will cease to be competitive in the short term and will not regain its competitiveness in the foreseeable future.

The TSBC does not support any effort by the Government to facilitate a further roll-out of gas, beyond which Tas Gas Networks is prepared to undertake, which it expects will be very limited.

73 AEMO, Gas Statement of Opportunities, 2013

74 7.30 Report, 15 August 2014, Tasmanian Minerals Council CEO Jeremy Kouw

75 Goanna Energy, July 2014 newsletter.

The TSBC is however very concerned that small businesses which have invested in conversion costs to natural gas will become unviable given the expected natural gas price rises and the costs of re-conversion, but notes that market interventions are usually very short lived, serving to delay increases rather than avoid them.

The TSBC notes that no component of the natural gas supply chain to Tasmania is regulated, and transmission, distribution and retail businesses will recover their costs and an appropriate profit margin, or become unviable themselves. Direct subsidy by the Government would involve a transfer of wealth from the broader community to a sector which has taken an informed commercial decision which has since been subject to changing market forces.

The TSBC therefore urges the Government to exercise caution in contemplating a market intervention, when there has been no market failure.. Such an intervention, if it were possible, would be expected to involve considerable cost which would be borne, depending on the intervention mechanism, by Tasmanian taxpayers or energy users.

The rising price of natural gas in Australia and the relevance of a gas reservation policy aimed at addressing that situation is a matter which the TSBC contends should be the subject of an informed public debate to which relevant stakeholders, including gas exporters, manufacturing industry and small business, can contribute. The TSBC is of the view that there appears to be a valid argument for intervention, due to market failure arising from the relative strength of the export sector versus local gas users, however there has been no genuine policy debate on the subject.

The TSBC recommends that the Government, through its Council of Australian Governments and Standing Council on Energy and Resources roles, plays an active role in bringing on that policy discussion.

Summary – question 12 and TSBC response

Is there a further facilitation role for Government in gas roll-out, or should Government focus its efforts on examining the costs and benefits of improving minimum protections for gas customers?

TSBC response:

The rapidly rising cost of natural gas and its impact on the viability of small business using gas is of major concern to the TSBC.

The TSBC does not support any effort by the Government to facilitate a further roll-out of gas, beyond which Tas Gas Networks is prepared to undertake, which it expects will be very limited

The TSBC urges caution before the Government considers investigating options to intervene in what is a fully commercial, unregulated market, with willing participants.

The TSBC recommends that the Government, through its Council of Australian Governments and Standing Council on Energy and Resources roles, plays an active role in bringing on a policy discussion concerning a gas reservation policy.

Question 13

What are considered to be the key opportunities, and the key issues, associated with possible energy futures?

TSBC response

In answering this question the TSBC has sought advice to identify the major drivers of change which will determine the energy futures (scenarios) which emerge which have the potential to impact the energy costs to small business, including for each driver:

- A description of the driver;
- A description of the desired future scenario;
- The challenges associated with achieving the desired scenario; and
- The opportunities associated with achieving the desired scenario.

The TSBC believes that a critical component of the Energy Strategy is the development of a range of credible scenarios, based on changes in the energy market and regulatory frameworks, together with outcomes which are influenced by Government decisions, which may then be subject to detailed analysis of predicted economic and social outcomes to inform those decisions which will deliver the best possible outcomes to small businesses.

Meeting the challenges identified in relation to each driver and taking advantage of the opportunities provides will enable delivery of the outcomes described in response to question 14 and provide the best opportunity for small business to prosper, along with the broader economy and community.

Each of the drivers discussed below will shape the scenarios which occur, and each presents challenges and opportunities, which will be the subject of government decision making. Those decisions will play a significant role in determining which scenario emerges in the future.

Change driver 1 – Oversupply

Projected electricity supply capability currently exceeds demand beyond 2023/24. Existing state owned electricity infrastructure is therefore underutilized and the return on assets to the Government is sub-optimal, with the risk that asset values will be written down as a result of regulatory processes or accounting rules.

Desired future scenario

Projected generation capability matches demand, with sufficient headroom to cater for hydrological risk and projected new entrant customers, allowing adequate time for delivery into the market of generation from new sources as required.

Challenges

- Loss of value resulting from the write down in asset values which should occur to allow prices to reflect a competitive response to the excess supply.
- Creating the right business environment to encourage new business to establish in the state, without the need to "pick winners".
- The potential loss of an existing major customer, adding to the existing challenge.

Opportunities

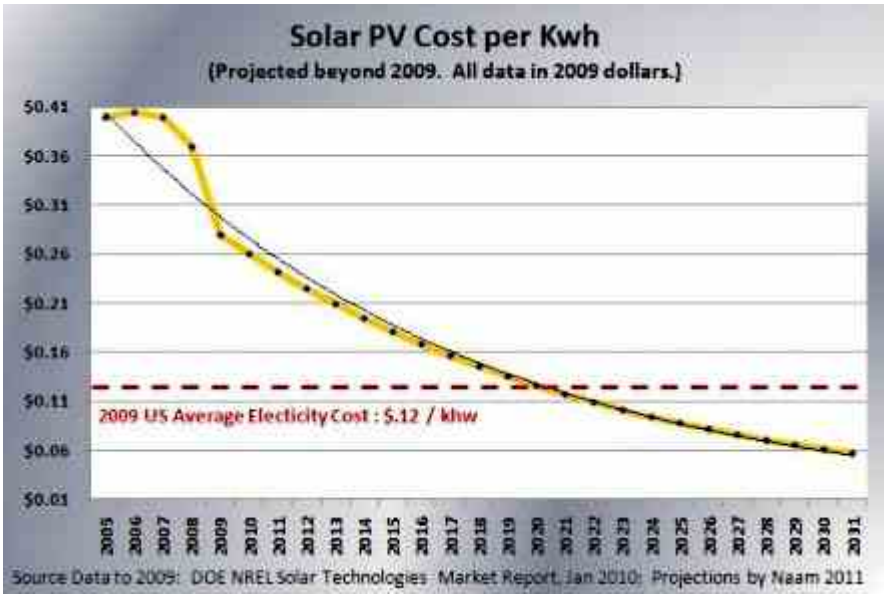
- Utilise the existing electricity to its maximum capacity, facilitating business and economic growth without the need for further investment.

Change driver 2- Electricity generation mix.

Over the next 20 years the supply/demand balance will change and, depending on the success or otherwise of attracting new, large customers, additional generation may be required in the medium and long term. The cost of gas fired generation will increase substantially over the next 20 years as east coast gas prices escalate under current projections.

Changes in the relative costs of other current options, including existing hydro, expanded hydro, wind, geothermal, biomass and interconnector options are not likely to vary substantially from their current relative costs. The relative cost of solar energy is however expected to reduce by around 50% by 2020, as suggested in figure 6 below:

Figure 8 Future cost of solar generation



Source – Eden News, Tue Apr. 30, 2013

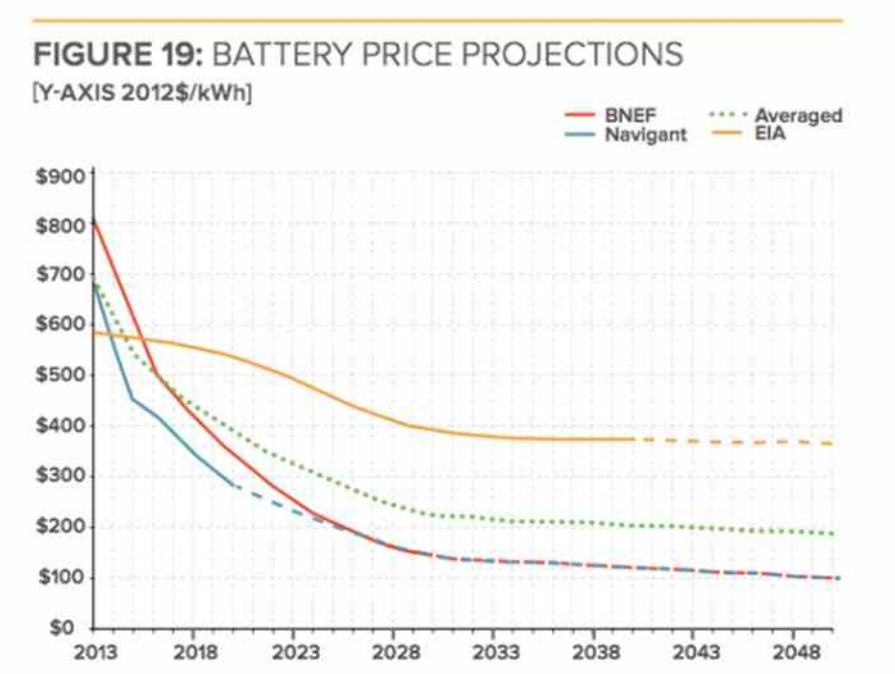
The TSBC expects there would be varying views on the relative cost of solar generation, which would need to be addressed in scenario modelling, however solar generation will without doubt impact future generation scenarios in two ways, being its attractiveness, including in combination with battery technology, to households and small business; and the commercial viability of large scale solar farms.

Large scale solar farms have a number of advantages over dispersed (rooftop) solar generation plant, including tracking capability, use of more efficient panels, more manageable impact on the network and more effective maintenance and replacement. Such solar farms could form part of base load for large customers (especially those providing large parking areas) or stand-alone generation.

The projected reduction in the cost of solar generation, coupled with the projected reduction in battery storage costs, poses a huge challenge to the current electricity delivery model and to the business model associated with that delivery

Figure 7 below provides a view of a number of industry players, including Bloomberg New Energy Finance (BNEF), Navigant, and the Energy Information Association (US).

Figure 9 Battery price projections



Source – Greentechgrid, Steven Lacey article, February 2014.

There are different views on the potential impact of solar PV/battery technology, however any participant in the electricity supply chain ignores that potential at their peril.

Battery (and other storage technology, such as flywheel or compressed steam) has the benefit of smoothing demand and helping to manage frequency variations. In the ancillary control services market within the National Electricity Market, that benefit attracts a payment. Coupled with the avoided cost of generation and network infrastructure, the deployment of solar PV/storage can be expected to become a viable alternative generation source, more cost effective than existing options, in a medium term scenario, and may dominate the electricity supply chain in the long term.

Conversely, the potential for gas to be used in embedded generation options is diminishing as gas prices increase.

Desired future scenario

The lowest cost mix of generation which meets security and reliability of supply requirements, installed at the optimum time to meet demand, and customers (large and small) enabled to choose low cost embedded generation which interacts with the electricity grid or stands alone.

Challenges

- Projecting future electricity supply and demand with sufficient accuracy to enable major investment (or sale) decisions. The variable with the greatest impact on demand to date has been the expanding penetration of rooftop solar PV generation, which can be expected to significantly increase as both solar PV and storage costs reduce. Other demand variables, as noted elsewhere in this submission, have been the increasing efficiency of energy utilisation, customer responses to rising prices and global financial crisis impacts.

- Development of price mechanisms to ensure an equitable apportionment of costs to all electricity consumers, that is, cost reflective with appropriate adjustment to reflect capacity to pay and other social considerations.

- Development of a new business (financial) model which:

    - Accurately reflects the growing risk of stranded assets as demand for grid-supplied electricity reduces;

    - Avoids the significant increase in unit costs for electricity supply which result from the current pricing model, which is in essence based on return on assets divided by volume, in an environment of reduced demand; and

    - Correctly allocates value to avoided cost and load smoothing.

Opportunities

- Reduce, in relative terms, the current cost of generation, taking account of all current costs including those attributable to under utilisation of existing plant.

- Use of private investment only to meet any future generation requirements, thereby avoiding government (including state owned business) funding implications.

Change driver 3- Technology.

The application of available technology, particularly in the in the transmission and distribution and home/business components of the electricity supply chain, is currently very small, compared to what is readily available. That technology includes, but is not limited to, smartgrid technology on the network (smart meters, advanced communications, real time condition monitoring, self-healing, automatic despatch, and load smoothing), and in homes and businesses - remote activated devices, home energy management systems, real time pricing with real time price advice to customers, customer information panels, and aggregated home energy management systems (where customers choose to outsource their real-time energy management to a third party).

Desired future scenario. Application of technology:

- Is optimised in the generation and network components of the electricity supply chain, based on positive business case outcomes, where benefits exceed costs.
- Is aligned with and enables accurate allocation of costs and benefits.
- Enables the desired level of customer information access, engagement and interaction, with the result that electricity is used as efficiently as possible, and customers pay an appropriate share of the cost of grid access and electricity consumption (total and peak demand).
- Enables customer choice.

Challenges.

- Selection of appropriate technology (communications, device protocols etc.).
- Providing information and education to customers to customers to enable them to choose their desired level of technology and interaction, and the cost implications.
- Development of mechanisms to ensure those customers who choose not to make use of available technology don't bear a share of the cost of deploying it.
- Getting the balance right between mandating the use and deployment of technology, thereby increasing the scale of deployment and reducing unit costs, versus an "opt in" model, which increases unit costs and costs per customer.
- Clarifying the roles, obligations, cost/benefit sharing, information access and physical access of existing market participants, new market participants and third party providers. In particular, cost and benefit sharing associated with load management (who controls the load, how are benefits identified, how are they shared, who incurs what costs).

Opportunities.

- Reduce operations and maintenance costs across the electricity grid.
- Enable customers to choose their generation options and/or reduce their electricity costs
- Reduce total demand and reduced peak demand, allowing avoidance or deferral of investment in electricity assets and thereby lower overall cost of producing and delivering electricity.

Change driver 4 – Climate change.

Whilst there might be doubt in some quarters as to the cause of climate change there is ample evidence to support the assertion that it is occurring. Electricity companies have experienced first-hand the impact of changes by way of increased frequency and scale of major events. For energy companies there are two major issues around climate change:

- Building energy infrastructure to cope with the effects of climate change, such as rising sea levels; and
- Responding to community expectations and political interventions to take action to reduce the energy industry's contribution to the cause of climate change (regardless of the veracity of the cause and effect proposition).

For example, given the 40 year expected life of most assets in the energy supply chain, the potential for sea level rises over the life of those assets and the possible scale of the rise is an important consideration in the location of new assets and in the maintenance and replacement regimes of existing assets.

Increasing energy efficiency, as a result of either customer choices, or targeted interventions, and schemes aimed at increasing the viability of renewable energy generation, each contribute to the changing demand profile and generation mix.

Desired future scenario.

Gas and electricity infrastructure is sufficiently resilient to the impacts of climate change to ensure that expected reliability performance is met, and greenhouse emission reductions and energy efficiency expectations of customers, the Government and other key stakeholders are met.

Challenges.

- Developing credible future scenarios of the impact of climate change, sufficiently robust to enable least cost asset management decisions and subsequent investments to mitigate the impact of the expected changes.

- At a policy level, determining Tasmania's position regarding interventions designed to impact greenhouse gas emissions or other climate change considerations, in addition to any which might be implemented at a national level.

Opportunities.

- An increased political appetite at a national level to intervene in markets in order to reduce the effect of greenhouse gases would, as has happened in the past, make renewable energy sources more attractive and lead to a broader mix of generation

than currently prevails. Tasmania's production of renewable energy would then, as it has in the past, become more valuable.

- The resulting investment outcomes may provide opportunities for local construction of renewable energy infrastructure, as well as installation.

Change driver 5 – The electricity supply business model.

The current business model for generation, delivery and consumption of electricity is changing and over the next 20 years will change dramatically. The current model is one of predominately large scale generation produced by a small number of generators, delivered by a network of "poles and wires" to customers, who then consume the electricity with, for the vast majority, little choice, control or information about their consumption.

That model is likely to be replaced by one where a large proportion of electricity is generated locally, including at the home or business with cost effective storage; the network serves as a "clearing house" where a very large number of generators wish to sell surplus electricity and an even larger number of customers are able to meet some but not all of their own demand and therefore wish to access the network to buy electricity; a large proportion of customers actively engage in managing their electricity supply and demand; and customers who do not wish to actively engage but are are able to access third party providers to manage consumption and cost on their behalf.

Under such a scenario, the current economic model, including network pricing based on the capital asset pricing model, will no longer be effective.

Desired future scenario.

Whichever business model for electricity supply emerges over the next 20 years must deliver:

- Safe, reliable and secure supply;
- Electricity delivered using the most efficient means possible (lowest cost) taking account of all constraints and contingencies, across all elements of the supply chain;
- Cost reflective outcomes – all consumers pay their fair share, subject to:
- An appropriate, transparent social equity framework; and
- Empowered customers with information to make informed choices and the capability to act on those choices.

Challenges.

- Providing policy makers with compelling arguments, capable of being translated and endorsed by a relatively uninformed public, which make sense out of what is already a very complex business.
- Engaging at all times with the public and key stakeholders on the transformation journey.
- Delivering social equity. Many customers will wish to remain uninformed, therefore the new business model will need to cater for that and deliver the right price outcome. The expectation of cost reflective pricing, user pays, will need to provide transparent support to low income earners and those who cannot afford new technology. Similarly there will need to be a balance between the cost of servicing rural areas under user pays principles, and price equity.

Opportunities.

- Development of the right business model, delivering the desired future scenario, will provide the opportunity to address the shortcomings in the current business model, the flaws in which are well known and force almost perpetual intervention in the regulatory framework as well as changes to achieve political objectives.
- Those which have not yet been identified. Development of the internet and mobile phones has delivered outcomes which were not possible to conceive when those technologies began. The same can be expected to happen as technology around electricity generation, delivery and consumption changes.

Change driver 6 – Electric vehicles.

The take up of electric vehicles in Australia and Tasmania has been very slow compared to other parts of the world, however that situation can be it can expected to change within 20 years. One estimate of electric vehicle take-up is 500,000 in NEM states by 2020. [76]

Most consideration of the impact of electric vehicles in Australia to date has focussed on additional network costs to manage the load associated with charging, however an alternative model would see electric vehicles as both a source of load and a source of generation. Under such a model, vehicles plugged in to charging devices and connected to the grid, via a home or business energy management system, would be re-charged at a time and volume dictated by either the electricity network operator or a third party load

76 AECOM, Impact of Electric Vehicles and Natural Gas Vehicles on the energy markets, final advice to AEMC, 22 June 2012.

management entity, with the objective of minimising the impact on the network and increasing utilisation.

Conversely, the network operator or load management entity would be entitled to access electricity stored in vehicles to provide load smoothing capability across the network, at both local and grid wide levels.

Under that model, electric vehicles would become a source of dispersed generation, as well as a dispersed load. Contracts with EV customers would include specified charge levels, to ensure the load management entity did not withdraw more than the minimum amount.

Desired future scenario.

The implementation of the model described above in a revised electricity supply business model, which incorporates energy management systems in homes and businesses, and also incorporates load management at local and grid wide levels, would be expected to deliver overall cost reductions in the electricity supply chain.

Challenges.

- Implementing the technology via a positive business case, ensuring the cost of electricity reduces rather than increases.
- Designing and implementing the new business model and supporting regulatory framework.

Opportunities.

- The AEMC estimated the mid-range take-up scenario of EVs to have the potential to deliver over $1 billion in savings annually across the NEM as a result of the improved load factor which would result if the EV charging load was effectively managed and delivered greater utilisation of network assets.[77]
- Tasmania currently imports all its energy requirements for domestic and industrial applications excluding the stationary energy sector. Conversion of a small percentage of the state's vehicle fleet would see a reduction in the reliance on fuel imports.
- The state's electricity generation and network assets have capacity to accommodate a significant conversion to electric vehicles from the current vehicle fleet.

77 AEMC (AECOM) IMPACT OF ELECTRIC VEHICLES AND NATURAL GAS VEHICLES ON THE ENERGY MARKETS, June 2012

Summary – question 13 and TSBC response

What are considered to be the key opportunities, and the key issues, associated with possible energy futures?

TSBC response:

The TSBC has sought advice on the future key drivers which will shape Tasmania's energy futures. Each of the drivers discussed will shape the scenarios which occur, and each presents challenges and opportunities, which will be the subject of government decision making. Those decisions will play a significant role in determining which scenario emerges in the future.

The TSBC believes that a critical component of the Energy Strategy is the development of a range of credible scenarios which may then be subject to detailed analysis of predicted economic and social outcomes to inform the Government's decisions.

Question 14

What could be some outcomes for the Tasmanian Energy Strategy, and what actions can government, or energy providers and consumers, take to achieve them? How could success/performance be measured?

TSBC response

The development and implementation of Tasmania's Energy Strategy and associated implementation plans, if properly designed and actioned, will deliver two major benefits to small business:

- Energy prices that are as low as they can possibly be, whilst meeting all of the Government's and the community's broader expectations; and
- A level of certainty around energy prices which facilitates long term business investment, absent from the current environment,

The TSBC is therefore very keen to play a role in ensuring that the Energy Strategy is of the greatest possible quality and guides informed and analysed decision making by Government and the State owned electricity businesses, and that the level of engagement with the business community and the broader community ensures the greatest chance that the agreed objectives are achieved.

The TSBC suggests that there are two perspectives of "outcome" which need to be considered. The first is the outcome which is the Energy Strategy itself - how it is developed, implemented and used to guide policy and investment decisions; and the second is the outcomes which are contained within the strategy, being the Government's, the community's and other stakeholders' objectives the strategy seeks to deliver.

The Energy Strategy

The strategy should include, among the other requirements as outlined in our response to Questions 11 and 12:

- Two sections, immediate/short term (1 to 5 years), including the recommendations of the Independent Review[78], and long term (6 to 20 years);

78 Electricity Supply Industry Expert Panel, An Independent Review of the Tasmanian Electricity Supply Industry, Vo1 1, March 2012

- An articulation of the drivers which will shape the change from the current scenario to a 20 year future scenario;
- A description of a number of credible future scenarios, including the external factors and Government decisions which have led to those scenarios;
- The results of economic modelling of each scenario against a range of parameters, including electricity prices, financial inflows and outflows to the State, and social equity outcomes;
- An assessment of the projected scenario outcomes against the desired outcomes, as discussed in the next section, which is used to guide Government and State owned electricity business decision making on strategic energy matters; and
- High level plans and timelines for the actions which the assessment above then guides.

As with the implementation of any long term strategy, success will be measured in two forms, the first being progress in delivering on the required actions and achieving milestones; the second in assessing whether or not the required actions delivered the desired outcomes, which necessitates the inclusion of measurable outcomes in the strategy.

Energy Strategy outcomes

The TSBC broadly endorses the outcomes proposed in the Issues Paper (p25) and comments as follows:

Objective 1. Tasmanian electricity prices will be sustainable and amongst the lowest in Australia

This objective should be achieved as a result of objective 2, efficient energy supply industries, an efficient regulatory framework and efficient and cost reflective pricing, not by way of Government intervention in the pricing process.

Objective 3.

Consumers will continue to have choices about how to meet their energy supply needs and will pay fair prices for those choices.

The TSBC strongly endorses this objective but reference to "*continue to have choices"* suggests that choice currently exists. For small business that is not the case. Small business does not currently have genuine choice about meeting their supply needs.

Objective 5.

Tasmanian businesses and households will achieve improved productivity and reduced costs through improved energy efficiency.

The TSBC notes that small business and households have that opportunity now, and would be expected to be aiming to reduce costs. A greater level of information and choice will enable the level of productivity improvement and energy efficiency to be increased.

Objective 6

The contribution of energy costs to cost of living pressures for the most vulnerable customers will be reduced.

As for objective one this should be achieved by improving the efficiency of the energy supply process, combined with more efficient use of energy, which will be enabled by better access to information and choice of supplier. The TSBC's position is that any support beyond that needs to be achieved by way of a social equity component in energy pricing which is fully transparent, and does not involve cross subsidy.

Objective 7

Economic development opportunities that are either enabled by energy supply, or are a result of direct energy investments, will create long-term economic growth.

The TSBC is of the view that this is a statement of fact which applies now. The Energy Strategy will not change that reality. The objective might be re-stated by adding to objective

Further comments

The TSBC notes the objectives proposed by the Expert Panel, following its investigations which are repeated at the end of this response for completeness[79], and recommends that these be incorporated into the Energy Strategy, along with the associated recommended actions.

In the introduction to this submission the TSBC proposed four principles which are fundamental to the Energy Strategy, being:

1. Energy is produced and delivered via the most cost effective means possible, noting that this must be over the long term, i.e. sustainable;

79 Ibid, p11

2. Energy consumption across all customer groups is as low as possible in order to meet customer requirements (thereby limiting the scale of investment in energy infrastructure and input costs);
3. The prices charged for energy to each customer group (or class) reflect the cost of production and delivery. (Implication – categorization of customer classes is appropriate, and there are no cross-subsidies).
4. Any variation of prices in order to achieve social equity outcomes is transparent and funding for any resulting subsidies is transparent and equitable.
5. All customers are empowered - with information about their energy use in a time frame (real time, monthly) which suits their needs; with the capacity to respond to the information as they choose; and with choices about how they use energy and who they purchase it from.

Principles 1 and 2 are reflected in the outcomes proposed in the Issues Paper, however the TSBC recommends the addition of principles 3, 4 and 5 to those put forward in the Issues Paper.

Actions Government can take

The actions taken by the Government need to be those which are specified within the Energy Strategy and associated implementation plans, other than those which are made to address short term issues which are not anticipated in the strategy, in which case those actions must align with the Strategy.

Measurement of performance and success

The TSBC suggests that the Energy Strategy should be viewed in the same way as any sound business planning process – a guiding strategy, subject to annual review (including key stakeholders as part of that review), with associated operational plans, which are subject to annual review and against which progress is regularly reported.

The TSBC therefore proposes that the implementation of the Energy Strategy should be achieved by:

- Treating implementation as a project or program of projects;
- Assigning a dedicated team, sufficiently well-resourced to do the job properly;
- Preparation of the usual project plans – risk management, stakeholder management, reporting framework, communications strategy, etc.
- The preparation of a high level implementation plan, which identifies who will do what, by when;

- As part of the reporting framework, a public reporting process, such as that employed by the Tasmanian Energy Regulator in the annual energy performance report[80].

How could success/performance be measured?

As noted above this should be in two parts:

- Reporting of progress against implementation plan milestones
- Once actions are fully in place over time to deliver each expected outcome, reporting of whether or not the actions delivered the expected outcomes. This would be by the inclusion in the Strategy of measurable targets. A small sample of those would include, for example:
    - an independent multi-dimensional assessment of the efficiency of State owned electricity businesses (as was conducted by the Expert Panel) against the current assessment;
    - the conversion rate of existing buildings to 5 star energy rating;
    - the rate of churn of retail customers;
    - the cost of energy in Tasmania compared to other states; and
    - the percentage of energy costs to total income for low income earners.

80 Office of the Tasmanian Energy regulator, Energy in Tasmania Performance Report

Summary – question 14 and TSBC response

What could be some outcomes for the Tasmanian Energy Strategy, and what actions can government, or energy providers and consumers, take to achieve them? How could success/performance be measured?

TSBC response:

The TSBC suggests that there are two perspectives of "outcome" which need to be considered: the Energy Strategy itself and the outcomes which are contained within the strategy.

The TSBC has proposed a broad structure/contents for the Energy Strategy, and recommends it be implemented by an appropriately resourced project team, guided by a comprehensive implementation plan.

The Government and key stakeholders will then be in a position to measure performance/success by:

- Assessing progress against the implementation plan; and
- Determining whether the Strategy's objectives have been achieved, by reference to measurable targets.

Expert Panel – suggested outcomes

Energy Supply Industry Desired Outcomes

1. An energy sector that is safe:
   - An industry that is safe for those who work in it and for the general community.
2. Energy supply that is reliable and secure:
   - There is sufficient supply (installed capacity and energy availability) to meet current and forecast demand.
   - An energy sector that provides the right energy source to meet energy needs within an efficient framework.
   - Network investment that is appropriate to ensure sustainability and reliability of supply.
   - The system is managed to withstand shocks.
   - Hydrological risk is appropriately managed.
3. An energy supply industry that is sustainable:
   - Environmental factors are appropriately managed (e.g. water resources and carbon emissions).
   - Energy supply industry participants are financially sustainable now and into the future.
   - Providers of capital investment achieve appropriate returns.
4. An efficiently operating energy sector:
   - Electricity generated by least-cost means at all times.
   - New sources of supply are triggered at the appropriate time.
   - Network services are delivered at least cost.
   - Retail functions are delivered at least cost.
   - Risks are appropriately allocated.
5. Transparent and appropriate management of energy supply risk
6. Prices that reflect objectives above:
   - Efficient prices – prices that support a sustainable industry (no more, no less).
   - Pricing structures that send correct economic signals.
   - Price movements that are predictable, that can be planned for and managed.

3 Summary of questions and TSBC responses

Question 1

What enhancements could be made to regulatory frameworks to ensure the right incentives for businesses and consumers are in place?

TSBC response:

Any further refinements to the existing regulatory framework, in the absence of an effective wholesale market, would add little value and would constitute tinkering at the edge.

TSBC notes the Government's 2012 decision to not accept the recommendations of the findings of the Independent Review of the Tasmanian Electricity Supply Industry, against input and advice from a range of sources including the TSBC.

TSBC strongly recommends the Government reverse that decision and progress to a competitive wholesale electricity market, which it expects will lead to effective retail competition and ultimately obviate the requirement for regulation of retail electricity prices.

Question 2

Given both the State and Commonwealth Government are committed to reducing red and green tape, and that the electricity market is highly regulated and complex, what opportunities are there to reduce or remove regulation?

TSBC response:

TSBC strongly recommends the Government should reverse its 2012 decision to reject the findings of the Independent Review of the Tasmanian Electricity Supply Industry in relation to the wholesale market structure in Tasmania.

Such a reversal would remove the considerable cost burden currently imposed on the electricity supply value chain in Tasmania as a result of the need to regulate wholesale and retail prices, translating to lower electricity prices for small business customers and all other customers.

The TSBC welcomes the opportunity to put its case to the Government, the Department or the Energy Working Group.

Question 3

Do energy intensive and trade exposed businesses require greater future price certainty to maintain and/or grow their operations?

TSBC response:

Yes, however the question of price certainty appears to stem from the very substantial increases to transmission prices over the last five years, as flagged by the MEU in its February 2014 submission to the AER.

The TSBC notes that small business has also suffered significant transmission price increases, as well as other increases across the electricity supply chain.

Any change to the Pricing Methodology applied by Transend which reduced transmission prices to MIs would be expected to have an opposite adverse effect on small business.

The TSBC suggests the Department should undertake a comprehensive review of Transend's (TasNetworks) Pricing Methodology, including asset values and load growth projections and the implications for future transmission prices.

Question 4

What enhancements or additional information could increase the reporting transparency of the Government's electricity businesses and contribute to improved efficiency?

TSBC response:

The TSBC:

Notes and endorses the conclusions and recommendations of the Electricity Supply Industry Expert Panel Review at Chapters 6 and 15 of Volume 1 and Part C of Volume 2.

Suggests the government should progress the recommendations at Section 6.8 as a matter of priority.

Proposes a number of key performance indicators applicable to TasNetworks which should be included in the proposed reporting regime, targeted at improving efficiency in areas where it believes there is currently substantial inefficiency.

Strongly suggests small business pays an appropriate share of efficient energy costs and is not forced to pay for electricity at a price which incorporates what amounts to hidden and substantial economic subsidies.

Proposes that Aurora should be compelled to report actual costs against allowed costs of activities resulting from the entry of new retailers, and that a pass back mechanism be developed for any over recovery.

Question 5

Do energy intensive and trade exposed businesses require greater future price certainty to maintain and/or grow their operations?

TSBC response:

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Question 6

Would you consider accepting slightly lower levels of reliability if this resulted in materially lower prices?

TSBC response:

Our members expect that efficiency gains, recent significant network investments and enhanced planning processes, will see reliability of supply improve, without extra cost.

We do not see ourselves being in a position to make a considered judgement as to whether the business value lost as a result of lower levels of reliability would be more than offset by the business value gained from reduced prices.

We note the development at a national level of a regulatory framework to enable that assessment to be made and we propose that the Energy Strategy should incorporate that development.

Question 7

Would a review of tariff structures be desirable, in terms of minimizing total network costs?

TSBC response:

Yes. Changing network tariff structures, with the resulting tariffs reflected in retail tariffs, will, over time, deliver lower electricity prices to all customers and will eliminate existing cross subsidies which do not favour small business.

Changes to network tariffs are part of a larger issue, being consumer engagement in managing their electricity consumption, and must be accompanied by changes in the way in which information about consumption and prices is provided to electricity customers.

We note the development at a national level of a series of actions to progress such changes and we propose that the Energy Strategy should incorporate that development.

Question 8

What approach, including non-regulatory ones, should Government consider for improving the thermal efficiency of our buildings?

TSBC response:

TSBC endorses in principle any proposal to reduce total energy consumption, reduce energy costs in the long term, and therefore reduce costs to small business.

Subject to the qualification that associated compliance or other costs imposed on small business do not exceed the demonstrable reduced energy costs and other benefits.

TSBC has proposed the structure of a five element scheme to deliver improvements in the thermal efficiency of Tasmania's building stocks and would be happy to discuss this with the Department or Energy Working Group.

Question 9

What approach to energy efficiency should Government use to help improve productivity for small to medium businesses, and to reduce energy bills for households?

TSBC response:

TSBC notes the work already in progress via the National Strategy on Energy Efficiency and Tasmania's response, including its Future Directions (energy efficiency) proposals.

TSBC proposes that the government should implement an energy efficiency program which is multi-dimensional, including information access, price differentiation, power factor improvement, direct funding and smartgrid development.

Directly funded sub-programs should only be implemented where demonstrable benefits outweigh implementation and other costs.

TSBC does not support the mandatory imposition of any energy efficiency scheme involving direct or indirect additional cost to domestic and small business customers.

Question 10

What role should Government play in attempting to retain and increase load growth in Tasmania and how should it do it?

TSBC response:

TSBC does not support Government intervention in the setting of wholesale or retail electricity prices for domestic and commercial customers in order to stimulate load growth, or to support the financial position of the state owned electricity businesses.

Competitive wholesale and retail markets are the TSBC's preferred options for price setting, which would over time deliver reduced electricity prices to small business and other electricity users.

In the absence of competitive markets the recently revised regulatory processes, administered by the Tasmanian Energy Regulator, must remain independent of Government.

Tasmania does have a range of competitive advantages which should be promoted by the Department of State Growth in its efforts to attract new business.

Question 11

What further potential is there to develop renewable energy in Tasmania, including wind energy, given there is no unmet Tasmanian demand requiring additional generation for the foreseeable future?

TSBC response:

Private investment in renewable energy, business case driven, will occur regardless of the current over supply situation, and can be expected to be mostly small scale, embedded generation. The payment of prices above avoided generation to solar photovoltaic generators is and will continue to contribute to the existing oversupply. Low cost solar energy is an emerging reality.

Any development of renewable energy by the Government or by state owned electricity businesses should be guided by the Energy Strategy and be subject to business case evaluation.

TSBC has proposed a broad outline of the contents of the Energy Strategy, which would include section one covering immediate challenges and actions and section two covering a description and evaluation of long term credible scenarios and actions associated with the most likely scenario.

TSBC recommends that the findings and recommendations of the Expert Panel's Independent Review should form the basis of the immediate challenges and actions section of the Energy Strategy.

Question 12

Is there a further facilitation role for Government in gas roll-out, or should Government focus its efforts on examining the costs and benefits of improving minimum protections for gas customers?

TSBC response:

The rapidly rising cost of natural gas and its impact on the viability of small business using gas is of major concern to the TSBC.

The TSBC does not support any effort by the Government to facilitate a further roll-out of gas, beyond which Tas Gas Networks is prepared to undertake, which it expects will be very limited

The TSBC urges caution before the Government considers investigating options to intervene in what is a fully commercial, unregulated market, with willing participants.

The TSBC recommends that the Government, through its Council of Australian Governments and Standing Council on Energy and Resources roles, plays an active role in bringing on a policy discussion concerning a gas reservation policy.

Question 13

What are considered to be the key opportunities, and the key issues, associated with possible energy futures?

TSBC response:

The TSBC has sought advice on the future key drivers which will shape Tasmania's energy futures. Each of the drivers discussed will shape the scenarios which occur, and each presents challenges and opportunities, which will be the subject of government decision making. Those decisions will play a significant role in determining which scenario emerges in the future.

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- Assessing progress against the implementation plan; and
- Determining whether the Strategy's objectives have been achieved, by reference to measurable targets.

Tasmanian Government

TASMANIAN ENERGY STRATEGY

SUBMISSION COVER SHEET

Please complete and post this form with your submission to:

Energy Strategy Submissions

Department of State Growth

GPO Box 536

Hobart TAS 7001

OR By email:

energystrategy@stategrowth.tas.gov.au

Name (first name and surname):	**Robert Mallett**

If submitting on behalf of a company or organisation:

Name of organisation:	**Tasmanian Small Business Council**
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- Submissions should be lodged by Monday 8 September 2014.
- Following processing, public submissions will be placed on the Department's website. The Department may decline to publish certain submissions (or parts of submissions) where there are issues concerning appropriateness or confidentiality.
- If the author of the submission wishes to exercise confidentiality in relation to a submission or a part of a submission, this should be clearly indicated, and will be respected.
- Where only parts of a submission are requested to be confidential, they should be submitted as an attachment to that part suitable for publication.
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- For submissions made by individuals, only your name and the state or territory in which you reside will be published on the Department's website. All other contact details will be removed from your submission.

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