PROPERTY COUNCIL of Australia

THE VOICE OF **LEADERSHIP**

Electricity Market Review Project Office
Public Utilities Office
Department of Finance
Locked Bag 11
Cloisters Square WA 6850

12 September 2014

Dear Steering Committee,

ELECTRICITY MARKET REVIEW

The Property Council of Australia welcomes the opportunity to provide comment on the *Electricity Market Review Discussion Paper* (the Review).

As the leading advocate for Australia's property industry, the Property Council represents the broad spectrum of businesses that own property, property developers, building managers and property industry service providers. Property Council members are among the top contestable electricity consumers in the Perth Metropolitan region and therefore take great interest in the competitiveness of electricity supply arrangements.

The commercial property market and the strata multi residential market represent a large portion of the existing contestable and non-contestable energy contracts held by the major retailers and, as a result, has driven significant competition within the contestable market. It is, therefore, of fundamental importance that the property sector is provided with a fair and equitable market within which it can participate.

Is the Market Delivering?

To some of the biggest consumers in the Perth Metropolitan area, the lack of competition among existing electricity retailers is noticeable. In the contestable market, most retail products include significant bias to the use of "pass-through" costs. These costs include capacity charges and renewable energy certificate charges, which are often portrayed as regulated charges, when in truth they could form points of competitive difference between retailers.

It appears that the portrayal of capacity charges as Government-imposed fixed costs is reflective of the retailers' view of the nature of the administered capacity mechanism (both in price and volume), and an inability or unwillingness to manage the risks imposed by a centrally administered arrangement.

Many retailers are also repackaging standard offer arrangements for generated energy from Synergy (formerly Verve). This significantly restricts the level of genuine competition in the only price segment that most retailers use to differentiate their retail offering.

The Property Council would support initiatives to increase the number of genuinely competitive retailers, including the potential for the structural separation of Synergy. We consider that a more vibrant retail market is required in WA to maintain genuine competition and that ultimately this will be of benefit to Government by driving out cost inefficiencies and lowering the level of financial support it is currently providing to Synergy.

Prioritise Private Ownership and Investment

The commercial property sector, by its ownership and investment in embedded network infrastructure, must be both acknowledged and protected in the Review. Through designing, commissioning and the ongoing management of large and small scale networks, the operators are effectively decentralising the network delivery and management. By engaging directly with the energy market participants, the property sector are actively utilising the mechanism's original design and the intent of the deregulated energy market.

Any change to the retail energy market in WA must not dilute or compromise ownership rights and or investment made by end users into their embedded network infrastructure and meter network assets. It is crucial that owners retain the right to recover fees to manage and maintain this infrastructure.

This approach encourages private investment by building owners and end users into current technology. Where this investment has occurred, significant efficiency improvements have been achieved in electricity consumption and peak demand.

Technology innovation in embedded network smart metering, and power quality improvement associated infrastructure is active within the property market, but limited in scale. The development of drivers, mechanisms and incentives to proliferate deployment of this current technology and innovation requires State Government input and assistance if this opportunity is to be exploited.

The capture of these efficiencies on a building or asset level reduces pressure on the SWIS capacity market, and can contribute to reducing the overall peak demand and capacity burden applied to the existing WP network infrastructure from the existing built environment.

The Capacity Market is Over Supplied

The Capacity Market is over supplied with falling demand and therefore the costs associated with this market are directly applied to the capacity charges imposed on retail energy contracts. The total annual cost of capacity in the WEM (price x volume) has increased 225% since the capacity year 2008/09. However the actual peak demand in the 13/14 capacity year (3,702MW) was only 6% greater than the summer peak demand in the 2008/09 capacity year.

The key drivers for these cost increase appear to be:

(i) Large pricing increases from the IMO methodology employed (+80%),

(ii) Peak demand forecasting errors, and

(iii) Excessive capacity certification.

Demand Side Management (DSM) alone accounts for approximately 550MW of capacity credits, which in itself exceeds the average capacity margin above the 10% POE forecasts in Table 2 of the Discussion Paper. DSM continues to receive increased capacity certification with corresponding payments despite an excess of resource capacity in the system. It is difficult to see the value that DSM is providing in these circumstances. The Steering Committee may wish to analyse the potential benefits of removing DSM as a resource from the capacity adequacy mechanism and allowing retailers to engage in these products directly, as a means of risk mitigation, and on a competitive basis. Alternatively DSM could be certified on a much shorter (1 year or less) commitment period.

The current inclusion of large block loads in peak demand forecasts is problematic, with loads that are inevitably difficult to define in both scale and timing. We support the concept of placing responsibility for procuring capacity for larger block loads directly on market participants and excluding these from IMO forecasting, as the WEM should not be taking on such project risk. We also support moving the responsibility for procuring capacity from the IMO to market participants, provided that an effective secondary trading mechanism is maintained.

We support the concept of an auction process or clearing house facility for available capacity as a means of putting downward pressure on capacity prices and to better manage excess or shortage of resources. Introducing market price signals should substantially improve the functioning of the current administered arrangement. We note that this approach follows overseas market trends, such as the new United Kingdom Capacity Market and north-east United States jurisdictions. Capacity auctions in the UK market will be held annually for capacity requirements 4 years ahead, as well as for one year-ahead adjustments. In the markets of the US north-east, each retailer is free to secure capacity either through self-supply or participation in an auction for sufficient resources to meet its capacity obligation. Forward periods vary from 3-5 years with shorter term "realignment" auctions.

Ultimately, high energy costs are imposed on the commercial property sector, with the great majority of the sector accessing the deregulated energy market on commercial bundled or unbundled energy contract arrangements. These contract arrangements are exposed to the full impact of high capacity charges and network charges. The commercial property sector in effect subsidises non-contestable tariffs via the impost of the oversubscribed capacity mechanism. Capacity charges are applied to contracted commercial properties accessing the deregulated energy market and in many cases property owners are on selling this energy to tenants at the artificially low gazetted tariff arrangements set by the State government.

Further, the increase of network charges, in some cases by greater than 9%, in recent years means the commercial property sector continues to pay greater than the protected non-contestable market.

Misdirected Electricity Subsidies

In many instances the State-controlled energy retailer allows large consuming government controlled buildings, educational facilities and community or NGOs' facilities to remain on non-contestable tariff arrangements. Frequently, new buildings are assigned the subsidised non-contestable tariff at first entry to the network with no adequate assessment or control measures to re-evaluate their load and adjust the applied tariff accordingly. As a result large businesses access subsidised non-contestable tariffs whilst commercial buildings on contract arrangements are exposed to the full cost pressures.

By incentivising, or at least removing misdirected subsidies, commercial buildings can significantly contribute to positive changes in the energy market and assist with the goal of the Energy market Review in reducing the high cost of energy and its provision on WA.

Review Recommendations

The commercial property and strata property markets must be recognised as significant contributors and stakeholders in the Western Australian Electricity Market. Their contribution to energy competition, efficiency programs and peak load reductions must be recognised and encouraged to expand and assist the aims of any electricity market reform in the future. Furthermore, as some of the top contestable electricity consumers, the property industry requires a reform to the current mechanism to reduce capacity costs, ultimately paid for by consumers, and introducing greater commercial flexibility for larger consumers.

The Property Council, therefore, supports reform that will encourage competition in a fair and consistent market without diluting or compromising ownership rights or investment made by end users. Ultimately, encouraging competition would be to the benefit of the government by driving out cost inefficiencies and lowering the level of financial support it is currently providing to the market.

Please find attached a confidential response to the discussion paper that is not for reproduction or circulation beyond those individuals involved in this review.

Should you wish to discuss the Property Council's submission further, please contact our Policy Advisor Rebecca Douthwaite on 9426 1203 or at rdouthwaite@propertyoz.com.au.

Yours sincerely

Joe Lenzo
Executive Director

Property Council of Australia
Ground Floor Parmelia House
191 St Georges Terrace
Perth WA 6000

P: +61 (8) 9426 1200
F: +61 (8) 9226 2865
ABN 13 008 474 422

E: wa@propertyoz.com.au
www.propertyoz.com.au