Australian Consumers' Association (ACA)
Submission to the
Independent Pricing And Regulatory Tribunal
of New South Wales

Inquiry into the Role of Demand Management and Other Options in the Provision of Energy Services - Interim Report
April 2002[1]

With reference to retail market driven demand management (Section 6.3 of the Report), we think there is a degree of lazy thinking by industry, regulators and some environmental advocates about price signals and consumer behaviour in the (electricity) marketplace. ACA supports conservation, minimisation of energy consumption, and reduction in green house gas emissions, and believes that it is important that 'green power' options and other conservation choices should be clearly represented and explained to consumers. However, in our view, many if not most consumers are likely to continue to choose an energy intensive life-style. Consumers will be expecting energy supply and security to be assured at an affordable price. An affordable price is not necessarily the cheapest possible, or even one that accords with the optimal economist model – it is one that fits into a framework of value expectations. One key expectation is that market reform should not lead to price *increases*. Energy is a consumer essential that on the other hand does not (yet) constitute a large proportion of the average household budget (although fuel costs can have highly regressive impacts on the budgets of low income consumers). Consumers may in general be relatively insensitive to optimised pricing in the sense of a competitive market price, but they are intensely interested in price stability and continuity of supply.

In our view the debate must allow for consumer choice. If consumers choose to consume, they should be accommodated in that - so long as the actual costs are appropriately signalled beforehand. Electricity billing takes place after the fact. Large bills may influence consumer behaviour, but since they come after the event (and in the case of the peak pricing of electricity, result from a fortuitous use of equipment at a particular time) they will also be greeted with outrage. It is basic to consumer protection that a person should know costs before purchase. If the intention is to influence consumers in a dynamic market, then their right to be informed about price before committing to usage must not be ignored.

Various players have been vociferous in their nomination of consumer use of air-conditioning (AC) as a major cause of problems. This is often accompanied by unconvincing expressions of concern for the equity implications of subsidy to AC owners by poorer electricity consumers. While it is apparent that the impact on average energy price from highly volatile AC load creates some cross-subsidy in favour of refrigerative AC users, a lot more needs to be done to quantify the level of cross-subsidy and its impact on low income and disadvantaged consumers. There are many other equity issues worthy of as much, if not more, attention.

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While the adoption of AC by consumers no doubt challenges the industry, it is generally fruitless to blame consumers for marketplace dynamics. The use of this equipment is a challenge for industry - to meet consumers' expectations. Equally, the expectation by consumers for enhanced bandwidth is a challenge for telcos - but we hear less "the sky is falling" talk in that domain. The telcos see this as a massive growth opportunity stemming from giving consumers more of what they want / need). Consumers purchase AC units as a legitimate product sold in an envelope of expectations, including the current pricing regime for power. These expectations need to continue to be met; otherwise there will be an explosion of consumer dissatisfaction. Price shock should be avoided. Air conditioning users vote and will not be happy if crude usage-based pricing is forced on them without an alternative - particularly when they have gone out and spent large sums (sometimes with electricity retailer subsidies) on an upmarket AC.

There seem to be hazards that the increased penetration of rarely used refrigerative AC will increase the average cost of electricity supply (in generation, transmission, distribution and retail). It takes a similar amount of capital to satisfy incremental load factors and the financial risks in the wholesale and retail energy market escalate dramatically during short periods of extreme demand stress. Volatility of wholesale price and risk skew the energy cost increase to consumers more than suggested by increases in demand. Similarly, slight decreases in demand at critical (short) time periods would allow costs and prices to fall. We accept that these extreme "needle" peaks will increase average energy costs to households and business consumers alike; and has the potential to increase the risk to reliable supply of energy (because in the South East regions of the NEM, the level of demand is less predictable within timeframes during which parts of the supply system may require maintenance).

But the critical point is that we are dealing here with needle spikes, not general demand growth. There are those who want price signalling to curb overall demand and demand growth, a bigger and more problematic agenda from the consumer point of view. It seems obvious that sensible load management could reduce the needle peaks and address many of the cost and infrastructure pressures, but still leave the question of general demand growth open. We would be far more comfortable with load and risk management initiatives that solve the acute problem, rather than broad brush pricing and metering approaches which may have significant unwanted and unanticipated effects.

There are serious structural issues to be settled on both the supply (genuine and transparent competition at all levels, national interconnection) and demand management sides (improved housing stock and consumer education) before blunt pricing signals are used in an attempt to modify consumer behaviour. In particular, heating and cooling loads are two forms of electricity use where short fluctuations in supply are likely to go unnoticed by consumers. Low-cost infrastructure is needed to allow effective (and automatic) load management "energy services" to be offered to consumers, such as interruptible and/or remotely switchable load. This could drive a lower cost outcome for all consumers. Interruptible or remote switchable loads would seem to be a better approach than crude user pays half hour price signalling or other variants that throw the risk onto the consumer.

We do not feel individual cost-reflective pricing and micro-metering is needed to deal with general demand growth. More energy efficiency building stock, energy efficient appliances/equipment, proliferation of more benign technologies (like gas-fuelled Fuel Cells etc), broad ranging consumer education and "conservation" incentives for consumers to cut consumption, will be more effective than average increases in prices. Consumers want risk management, continuity of supply and price stability. Industry and regulators need to make sure they get them. Indeed this is an opportunity to offer load management services to consumers that would help industry reduce the drivers pushing increased costs. There is a need to examine critically the limitations of crude price signalling on the variable use component of capital intensive, fixed cost heavy industries as a strategy to change consumer behaviour. Actual charges related to electricity consumed, as opposed to covering fixed costs of generator plant, distribution and retailing are comparatively low. Inflating the usage component will lead to increased pressure to unbundle fixed costs. Indeed in a capital-intensive industry, the commercial emphasis and imperative will increasingly be on recovering fixed costs with standing charges unrelated to usage. Expecting environmental and other outcomes from usage related price signals will be like pushing on a piece of string.