

18 May 2020

Energy Security Board

By email: info@esb.org.au

Re: Response to Consultation on Two-Sided Markets

Spark Infrastructure has interests in some \$18 billion of electricity network assets, delivering energy to more than 5 million customers across the National Electricity Market (**NEM**). These interests include a 15% interest in TransGrid, the electricity transmission network in NSW, a 49% interest in South Australian Power Networks, the electricity distribution network in South Australia, a 49% interest in both CitiPower and Powercor, two of the electricity distribution networks in Victoria and 100% ownership of the Bomen Solar Farm in NSW.

Our interest in the Energy Security Board's (**ESB's**) post 2025 NEM design is to ensure an efficient and effective market that provides incentives to investors to provide the right investment at the right time and in the right place. Importantly, the market must avoid introducing additional risk and be resilient to government intervention. This will deliver the lowest cost of capital and as a result, the lowest cost electricity to customers when they need it and where they need it. We support the use of markets and efficient pricing signals to incentivise the investment required to operate the system and sustainably deliver services to customers.

The need for change to better orchestrate the changing generation mix and the way customers use networks and services is apparent. The grid should support the efficient exchange of energy and the regulatory framework must evolve to better reflect the outcomes valued by customers. This will include changes to enable and incentivise the shift from one-way transportation of electricity from centrally located generation plants to two-way flows of electricity between consumers, new services, and continued innovation.

Two-sided markets provide a platform to optimise the integration of markets for essential system services and ahead markets that will better support the operation of the system, efficient matching of supply and demand, and the efficient delivery of system requirements and services to customers. We agree that these reforms can deliver benefits such as lower prices, choice and desired system operating conditions.

However, the experience in the NEM to date is that where prices have risen, government and regulators have intervened to reduce prices, removing the incentives for investment and increasing risk to investors. As a result, investment in renewable generation has fallen significantly and investment in networks is at an all time low. If prices are relied on to provide incentives for the investment required to meet demand and ensure the system operating requirements are met, the resilience of the reforms to government and regulatory intervention must form part of the evaluation process.

Therefore, to maximise the effectiveness of these markets to deliver desired outcomes, they must be accompanied by:

- Government support for pricing reform and targeted initiatives to support customers that need protection from adverse pricing outcomes to reduce the propensity to intervene; and
- Strong governance processes for making changes to the market arrangements so participants can confidently interact in the market and reduce the likelihood of intervention.

The benefits will require efficient price signals to be passed through to end-use customers

Pricing reform and targeted support for customers will be necessary to support two sided markets because two-sided markets will result in more consumers being exposed to efficient market pricing signals. Although efficient price signals should result in a lower cost system which reduces prices to all customers, prices to some customers may increase. Therefore, we recommend accompanying the move to two-sided markets with a package of targeted government initiatives to support those customers that need it. This will reduce the cost of providing the support whilst avoiding the need to dampen signals and protect customers that do not need it. As a result, existing non-pricing customer protection arrangements can be relied on rather than introducing arbitrary prohibitions on certain customer groups from participating in the market or regulating prices.

Strong governance processes are necessary to avoid unnecessary additional risk and cost

The propensity and likelihood for government to intervene in markets will increase risk and reduce participation. Strong governance processes characterised by clear objectives, robust cost benefit analysis, transparency and external review will improve stability, predictability, and confidence in the market. Establishing clear processes for when, how and why government and regulators can change the arrangements will be critical to maximise participation of both suppliers and consumers in the market. Maximum participation will also maximise benefits and avoid introduced distortions.

Amalgamation of related reforms

We have actively followed the AEMC's COGATI Access and Charging proposals to introduce locational marginal pricing (**LMPs**) and financial transmission rights (**FTRs**). We have expressed our reservations that these reforms will not deliver benefits that outweigh the additional complexity and cost compared to the current strong signals to investors from loss factors and constraints. Further, we have concerns that these reforms may increase the cost of capital for new generation (and therefore the costs to consumers) which was a common view revealed in the AEMC's investor survey. Therefore, we would urge the ESB to assess the interaction and duplication of reforms such as two-sided markets and resource adequacy mechanisms with LMPs, and FTRs as well as the incremental costs and benefits of each mechanism.

We also consider the important work being undertaken by AEMO, Energy Networks Australia (**ENA**) and ARENA to identify the regulatory and legal constraints, and the costs and benefits associated with integrating distributed energy resources is directly relevant to the design, transition, and implementation of two sided markets. This work includes relevant information on pricing options which should be considered alongside the 'subscription' approach to network pricing outlined in the paper and the work of the ENA and AER on successfully progressing network tariff reform.

I would be happy to discuss these matters further and can be contacted on 0421057821.

Yours sincerely,



Sally McMahon
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