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User Participation Working Group
C/- Office of Energy Planning and Conservation
GPO Box 936
HOBART TAS 7001

Improving User Participation in
the Australian Energy Market
Discussion Paper March, 2004

Dear Sir/Madam,

I refer to the MCE discussion paper for Improving User Participation in the Australian Energy Market dated March 2004 and provide the following comments.

Esso Australia Resources Pty Ltd ("Esso"), a subsidiary of ExxonMobil Corporation, is a producer of gas from the Gippsland basin in Victoria. Esso's gas from Gippsland is supplied to customers in Victoria, New South Wales, Tasmania and South Australia. In addition, affiliates of Esso are seeking to be gas producers in PNG and the Carnarvon Basin, offshore of Western Australia. The PNG affiliates are part of a group marketing gas into the north and east of Australia for a project that, if implemented, will require the development of a major new greenfields transmission pipeline from PNG to the southern Queensland and eastern Australian markets. The marketing focus for Carnarvon Basin gas is on export LNG sales and on future domestic gas sales opportunities in Western Australia that are reliant on the existing transmission and distribution infrastructure and the efficient future development of that infrastructure.

ExxonMobil affiliates are also major consumers of electricity at petroleum refining and storage facilities, with consumption around 170 GWh, and cogenerators of electricity at the Longford oil and gas production facilities with net exports to the national grid of approximately 100 GWh per annum.

As a major Australian gas producer and participant in the Australian gas industry, and as a major electricity consumer and cogenerator, Esso has a significant interest in the restructuring of the energy regulatory environment. Esso believes that critical to the supply of energy to the Australian markets is an efficient and competitive energy industry and an efficient regulatory environment.

An ExxonMobil Subsidiary

In its consideration of User Participation in the Australian Energy Market, the working group, has identified three areas for consideration; Options to Encourage Demand Side Response in Energy Markets, Interval Meters, and Retail Pricing. Esso believes each of these areas must be studied and are essentially interlinked. However, Esso believes that the Retail Pricing study scope should more fundamentally review the need for price caps and the benefits they provide, rather than simply focussing on how price cap levels should be set and transparency of process.

Encouraging Demand Side Response

For the development of a mature and competitive economy in south eastern Australia it is important to ensure the energy market can deliver the most efficient outcomes into the future. Clearly market competition and efficient development will be facilitated through demand side responses as competitive alternatives to supply side investment. Such demand side responses can only occur if there is a more direct link between consumers and the wholesale market either through direct market participation in a demand side response pool, or through a demand side aggregation facility. In either case, it is vital that the costs of participation and in particular, regulatory overhead are minimised to ensure they do not present a barrier to participation. Esso would encourage the SCO to conduct their proposed additional demand side aggregation work and to review the level of regulatory overhead as a potential barrier to participation.

Interval Meters

The electricity supplies to Esso's facilities are under contract arrangements and therefore interval meters are installed. Esso believes that interval meters can be valuable for large industrial customers, although the degree to which demand processes can be shifted to offpeak periods will very much depend on the individual business and process. Esso expects that analysis is likely to show a negative cost / benefit for interval metering for the retail customer sector because any material benefit would require significant behavioral change with respect to the use of air conditioning.

Retail Pricing

Esso contends that implementing retail pricing controls is not an appropriate approach to enhancing user participation. In fact, Esso believes a significant factor overshadowing the ongoing development of a competitive south eastern Australian energy market is the State Government imposed price capping in the retail electricity and gas markets.

Price caps pose a substantial risk to the long-term health of the energy market. Price caps negate vital supply versus demand signals reaching substantial consumer sectors that would otherwise drive efficient market solutions either through demand side responses or investment in new supplies. If a situation arises where the cost of potential new or replacement supply increases and consumer prices have remain capped, either market failure is a likely outcome or the consumers and market will suffer a substantial price shock.

Current electricity and gas supplies in south eastern Australia utilise existing infrastructure that was in large part put in place over the past 30 years. Substantial new investment in both electricity and gas infrastructure will be required to meet demand with demand side response having the potential to impact the timing. In the case of gas, as developed reserves in the Gippsland and Cooper basins run down, new investment will be required in these fields and others to maintain supply. It is therefore vital that clear market signals connect demand and supply in key energy markets.

Esso believes the appropriate course of action is to remove retail price caps and allow competition between alternative gas supplies, and between gas and alternative fuels such as electricity, LPG and distillate.

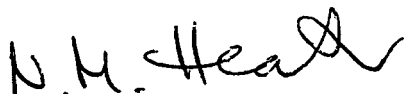
Esso believes the continued existence of capped retail prices will, over time, prevent new electricity and gas supplies entering the market and the retail market will eventually face shortages.

Esso supports the need for a national framework whereby the need for price regulation for certain consumer groups and in certain jurisdictions would be reviewed on a regular (perhaps biannual) basis by a national body independent of the individual State political environments. Price regulation should only be implemented or maintained where there has been found to be a market failure through the breakdown of normal competitive forces such that, a net public benefit may be demonstrated. Any such review must consider the total energy market perspective and correctly consider the competition provided by all forms energy (gas, electricity, LPG, liquid fuels, coal, etc.). In jurisdictions and for consumer groups where there has not been such a market failure, price regulation should only take the form of Government subsidies for under-privileged groups in the community. Where market failure has been demonstrated, regulators should in the first instance consider a price monitoring regime rather than price regulation. Where price regulation is imposed as a secondary response, it is important that it recognise the full cost of service to ensure consumers are not isolated from market signals.

Esso thanks the User Participation Working Group for the opportunity to comment on the discussion paper for Improving User Participation in the Australian Energy Market and will look forward to commenting further as the MCE conducts further studies and develops more detailed proposals.

If you have any questions regarding this submission or would like to arrange a time to discuss it further please do not hesitate to contact me on (03) 9270-3457 or you can contact Nigel Collins on (03) 9270-3682.

Yours sincerely,



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