

19 December 2013

Mr John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
SOUTH SYDNEY NSW 1235
Lodged online at www.aemc.gov.au

Dear Mr Pierce

Response to AEMC Consultation Paper on Distribution Network Pricing Arrangements

ActewAGL Retail welcomes the opportunity to respond to the AEMC's *Consultation Paper, National Electricity Amendment (Distribution Network Pricing Arrangements) Rule 2014* (consultation paper). ActewAGL Retail is a public-private partnership owned equally by ACTEW Corporation and AGL Energy. ActewAGL Retail provides electricity and gas retail services in the ACT and south east New South Wales.

ActewAGL Retail is required under section 22 of the *National Energy Retail Law* to offer ACT customers who consume less than 100MWh per year of electricity a non-negotiated standard customer contract incorporating a tariff approved by the Independent Competition and Regulatory Commission (ICRC). These customers are known as franchise customers. ActewAGL Retail also offers market based tariffs to non-franchise customers.

The rule changes proposed by the Independent Pricing and Regulatory Tribunal (IPART) and the Standing Council on Energy and Resources (SCER) would result in significant changes to the network tariff approval process and to the structure and level of network tariffs.

ActewAGL Retail considers that some of the proposed changes to the tariff approval process may assist retailers and customers, by giving them more time to understand and respond to changes in network tariffs. However we are concerned that the proposed changes to the network pricing principles would result in more complexity, uncertainty and increased costs for retailers and consumers, particularly in those markets such as the ACT which remain subject to the constraints of retail price regulation.

The network tariff approval process

Earlier finalisation of the annual network pricing approval process, as proposed by IPART, would be helpful as it would give retailers more time to respond to changes in network tariffs, set their retail tariffs, adjust billing systems where necessary, and notify customers (as required under NECF), before the changes take effect. However we are also advised that there are risks and practical difficulties involved with earlier notification, particularly in the first year of a new regulatory period, where the AER's determination on distribution network prices is usually finalised only a short time before the prices take effect.

The proposed rule changes also aim to create more certainty and predictability for retailers and consumers through a new process whereby distribution network service providers (DNSPs) would be required to prepare a Pricing Structures Statement (PSS) and submit it to the AER as part of the 5-yearly regulatory determination. ActewAGL Retail believes that a high level statement setting out and explaining DNSPs' proposed tariff strategy for the next 5 year regulatory period could play a useful role in providing information and a basis for consultation with retailers and consumers. However, there is a risk that by being bound to the tariff structures and levels set out in the PSS, for a period of up to 5 years, DNSPs may not have enough flexibility to respond to rapidly changing circumstances and this would have implications for all stakeholders in the price setting process. Energy markets are constantly changing, often in ways that are difficult to predict, and it is in the long term interests of all market participants to have some flexibility in tariff setting. The need for flexibility is recognised in NECF requirements as retailers in the ACT are able to change standing offer prices once every 6 months.

ActewAGL Retail agrees with the AEMC on the importance of consultation in relation to network tariffs. Consumers and retailers need to understand proposed network tariff changes, and be given opportunities for consultation with DNSPs. However, we believe that prescriptive rules or guidelines on the nature and frequency of consultation are not necessary, and may impose an additional burden on retailers, consumers and DNSPs, for no clear net benefit. The AER's recently released consumer engagement guidelines provide an appropriate high level framework for consultation on network pricing matters.

The distribution pricing principles

The likely impacts of the proposed changes to the pricing principles are difficult to determine at this stage from a retail perspective, given the high degree of uncertainty about their practical application, particularly the proposal to mandate that network prices be "based on" long run marginal costs (LRMC). We understand that a range of methods, definitions and assumptions can be applied in calculating LRMC, and the approach taken will influence the estimates. As the Productivity Commission has pointed out, once LRMC has been calculated, it can be incorporated in charges in several ways — including volumetric charges, access charges, charges linked to a customer's maximum demand, and targeted charges based on particular demands placed on specified parts of the network (such as a localised substation or neighbourhood feeder).¹

¹ Productivity Commission 2013, *Electricity Networks Regulatory Frameworks, Inquiry Report*, volume 2, April, p. 437

Overall this suggests that a requirement for distribution network tariffs to be “based on” LRMC would likely result in more complex and variable network tariff structures, potentially with location elements and charges to reflect LRMC at a highly disaggregated level. The LRMC definition suggested in the consultation paper refers to costs “to meet a particular user’s” demand.²

A more complex network tariff structure, explicitly designed to more accurately reflect differences in costs across users, locations and times seems to require considerable thought and assessment prior to implementation and we would require sufficient time to assess the implications for tariff structures and levels from a retail perspective. ActewAGL Retail suggests that the AEMC should undertake detailed modelling and analysis of the potential implications of mandating that network prices be based on LRMC and if possible provide a guide to retailers of the likely implications of such changes.

ActewAGL Retail notes that it would be concerned though at any possible inference underpinning the setting of network tariffs on a LRMC basis that retailers should be required to preserve such network pricing signals in retail prices. Retail electricity prices should be free of price regulation and the competitive market should be allowed to drive commercial pricing solutions that best meet the needs of customers.

ActewAGL Retail looks forward to continuing engagement with the AEMC during the review of the rule change proposals. Please contact me on (02) 6248 3308 if you would like to discuss any aspect of our submission.

Yours sincerely



Ayesha Razzaq
General Manager

² AEMC 2013, *Consultation paper, National Electricity Amendment (Distribution Network Pricing Arrangements) Rule 2014* (Consultation paper), p. 58