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Dear Mr Pierce, *John*

**SUBMISSION TO AEMC'S CONSULTATION PAPER - PROPOSED RULE CHANGE -
DISTRIBUTION NETWORK PRICING ARRANGEMENTS**

Thank you for the opportunity to comment on your Consultation Paper on distribution network pricing arrangements. IPART remains supportive of our Rule change proposal submitted in September 2012 for the reasons that we have previously articulated.

We also support SCER's proposal to base network prices on an estimate of the long run marginal cost (LRMC). However, we would like to see some analysis on the impact of moving to LRMC based prices and how that relates to current prices.

In NSW relatively few customers have time of use meters. For customers on accumulation meters where there is no local capacity constraint, the variable charges are likely to be low with high fixed charges. For such customers the transition to LRMC based pricing needs to be managed.

Further, we consider that SCER's proposed changes to the pricing principles:

- ▼ places more significance on addressing both the timing and consultation aspects of our Rule change proposal, and
- ▼ reinforces the need for consultation to cover both the structure and level of prices.

Please contact Anna Brakey on 9290 8438 or John Smith on 9113 7742 if you have any queries in relation to the submission.

Yours sincerely



Peter J. Boxall AO
Chairman

Annual network pricing arrangements – Rule change proposal

Submission on AEMC's Consultation Paper
December 2013

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1 Introduction

In September 2012, IPART proposed changes to the National Electricity Rules (NER) to set network prices:

- ▼ with greater consultation, to allow customers to better understand any proposed changes and to provide retailers with greater opportunity to understand the impact of any network changes on their pricing strategies and to develop their retail prices, and
- ▼ earlier, to allow sufficient notification of network price changes.

IPART continues to support our Rule change proposal for the reasons set out in both our proposal and our submission to the AEMC's June 2013 Consultation Paper. Since we made the Rule change proposal, the National Energy Customer Framework has commenced in NSW, which in our view increases the urgency for changes to the network pricing arrangements in the Rules.

The Standing Committee on Energy and Resources (SCER) has subsequently proposed changes to the NER to address consultation arrangements in a similar manner to the IPART Rule change proposal. The SCER proposal also addresses pricing principles, but it does not address the timing aspects raised in our Rule change proposal.

The Australian Energy Market Commission (AEMC) has consolidated these proposals and released a further Consultation Paper.

2 Proposed Rule changes

We support SCER's proposal to base network prices on an estimate of the long run marginal cost (LRMC). However, we would like to see some analysis on the impact of moving to LRMC based prices and how that relates to current prices.

In NSW relatively few customers have time of use meters. For customers on accumulation meters where there is no capacity constraint, with network tariffs that reflect LRMC the variable charges are likely to be low and the remainder of the revenue requirement would be recovered through relatively high fixed charges. While this could benefit large consumers of electricity, it could have a significant impact on small users. This transition needs to be managed appropriately.

Further, we consider that SCER's proposed changes to the pricing principles:

- ▼ place more significance on addressing both the timing and consultation aspects of our Rule change proposal, and
- ▼ reinforce the need for consultation covering both the structure and level of prices.

Where there are significant customer impacts we recommend that a transitional approach be adopted. To implement this transition, we recommend that the AEMC consider a 'target tariff' approach. Under this approach, the DNSP would be required to set out both the level and structure of its charges under the revised pricing principles, and be required to move its current prices towards those target tariffs in a manner that accounted for customer impacts.

3 Our response to specific questions raised in the AEMC's Consultation Paper

This section responds to specific questions raised by the AEMC where IPART can make our most relevant contributions. We have not responded to every question posed by the AEMC.¹

Question 2 – does Figure 6.1 reflect the key components of how network tariff structures and pricing levels [are] determined by DNSPs?

No - we consider that Figure 6.1 does not adequately recognise the relationship between network price structures and levels, with the process being iterative and integrated. Further, we consider that there is a relationship between the network costs and the price setting process, which is not recognised in Figure 6.1.

¹ The AEMC refers to the equivalent of our Statement of expected price changes as the Pricing Structure Statement. We have continued to call it a Statement of expected price changes as we consider that it should include both structures and levels.

Question 4 – What level of information on network tariff structures and network tariff pricing levels should be included in a network tariff structures document to assist retailers and consumers to understand and respond effectively to changing prices and structures over the regulatory period?

The statement of expected network prices should include information on both the structure and level of expected prices. Both are crucially important. As highlighted by the retailers at the AEMC's public forum, a document that included structure is not a substitute for knowing the level of prices.

Question 5 – Should DNSPs be able to vary their network tariff structures during the regulatory period? Why or why not?

Yes – DNSPs should be able to vary their network tariff structures during the regulatory period. This will allow them to respond to changing circumstances. However, we consider that the DNSPs should consult with customers and retailers on changes to the document.

Question 6 – If a document on network tariff structures is put in place, should this be an indicative document or should the DNSPs be required to apply it in their annual pricing proposals?

The document on network tariff structures should be required to apply in the annual price setting proposals – this will make the statement of expected price changes a meaningful document. However, we consider that it is important to provide the DNSP with sufficient flexibility to alter its statement of expected network prices during the regulatory period.

Question 7 – If a document on network tariff structures is binding on the DNSP, should it be able to be varied and under what circumstances? If so, should it be varied outside or within the annual network pricing process?

Yes, the document should be able to be varied during the regulatory period. The DNSP should be able to vary it to take account of changing circumstances. It should be changed in consultation with customers and in advance of the annual network pricing process, as proposed in IPART's Rule change proposal.

Question 8 – Should DNSPs be required to consult with stakeholders before submitting their proposed pricing structures statement to the AER for approval through the regulatory determination process?

Yes - the DNSPs should be required to consult with stakeholders in developing or changing their statements of expected price changes. While we consider that the consultation should take place at the time that is most useful to the networks, retailers and customers, we note that the statement cannot be finalised until the network revenue process is finalised due to the requirement to include levels in the document.

We note that the AEMC set out the purpose of consultation in its Consultation Paper, stating "... the purpose of the consultation is to determine consumer impacts from the proposal network tariff structures ...".² However, we consider that the purpose of the consultation is broader, providing:

- ▼ greater input from retailers and customers in developing network prices
- ▼ a clear path over the regulatory period to ensure that all stakeholders have access to information on how network prices will move
- ▼ more time for retailers to make any necessary changes to billing systems and engage with customers about upcoming changes in network prices
- ▼ improved functioning of the retail market.

Question 9 – Is consultation on amendments to the pricing statement necessary during the regulatory period? Are there circumstances when it would not be necessary?

Yes – we think that consultation should generally be required in amending the pricing statement during the regulatory period. However, there could be circumstances where consultation may not be necessary (for example, a straight pass through of a certain change in costs) or could be proportionate. This would ensure that the costs of consultation are minimised where appropriate.

Question 11 – Should the AER be required to provide guidance on the consultation process for DNSPs? Should the guidelines be binding on the DNSPs?

Yes – we have proposed that the AER establish the requirements for the content of the statement of expected network prices, including the requirements for consultation. The guideline should be binding. In developing the guideline, the AER could provide for proportionate consultation in certain circumstances.

We consider that this detail is best dealt with in a guideline rather than in the NER to more easily facilitate changes to ensure that the document and process remains relevant to stakeholders.

Question 16 – Should DNSPs include forecasts of their expected changes in network tariff pricing levels in the pricing structures statement?

Yes - we strongly recommend that levels be included in the statement of expected prices. We see the price levels as being as important as structures.

For example, if a DNSP seeks to increase the fixed price significantly in a year, then customers and retailers should be provided with advance notice. Retailers will then be able to engage with their customers to let them know of the changes.

² AEMC, *Network Electricity Amendment (Distribution Network Pricing Arrangements) Rule 2014, Consultation Paper*, 14 November 2013, p 39.

Further, if a DNSP would like to introduce a new tariff structure (say a demand based charge), then it will matter to the retailers and customers whether this is a significant component of the bill.

We consider that the changes to the pricing principles proposed by SCER places greater emphasis on including levels in the statement of expected price changes.

Question 17 – Should any changes to the network tariff pricing levels included in the pricing structures statement be subject to consultation? If so, what level of materiality should apply to the change?

Yes, we consider that changes to the network pricing levels should be included in the statement and subject to consultation. We think that if a level changes by more than 10% over previous estimates, then it should be consulted on. This threshold will ensure that consultation remains proportionate and contains costs.

Question 20 – If the [statement of expected price changes] were implemented, would this reduce the timing pressures for the DNSPs, the AER and retailers that have arisen from the first year and subsequent year annual pricing process?

Yes, we anticipate that the proposed changes will reduce timing pressures to an extent. However, we do not see the statement of expected price changes as a substitute for the changes to the timing provisions set out in our Rule change proposal. Rather, our proposed changes to the timing and consultation provisions complement each other.

We note the inconsistency in procedural requirements for notification of price changes between the NER and National Energy Retail Rules in relation to the timing of network price approval and the notification by retailers to their customers of price changes (as described in our previous submission). We consider that the AEMC, as the Rule change body for both sets of Rules, should address this inconsistency.