

Overview of the draft rule: Distribution pricing principles

Public Forum: Distribution Network Pricing Arrangements draft
determination - 22 September 2014



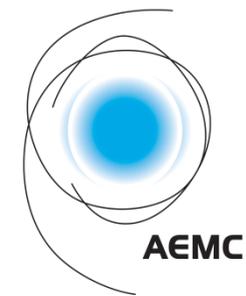
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OVERVIEW OF THIS SESSION

- Provide an overview of the draft new network pricing principles.
- Explain the rationale behind some of the changes.
- Responses to the proposed changes from representatives of different stakeholder groups.
- Discussion at the conclusion of the presentations.

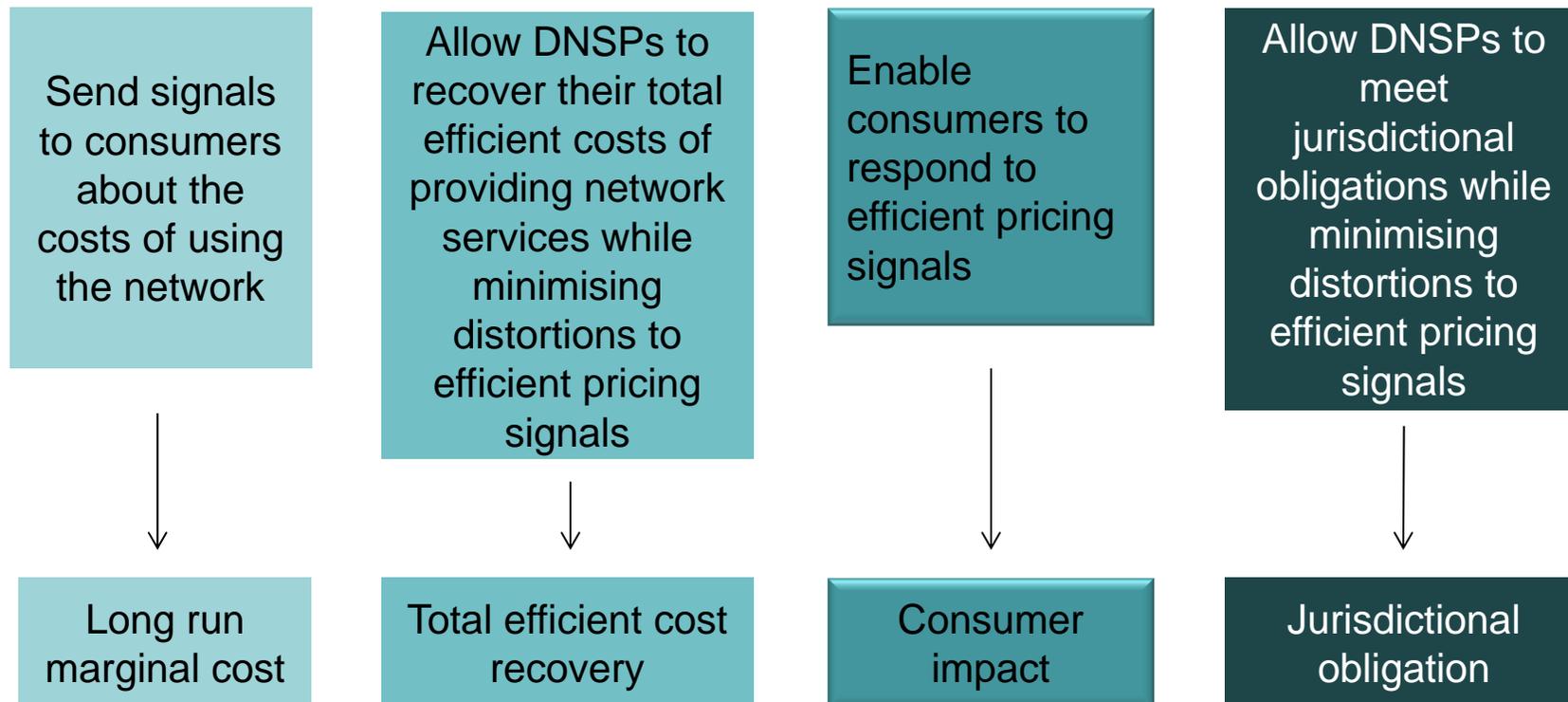


DISTRIBUTION PRICING PRINCIPLES



Pricing principles

Network pricing objective: tariffs that a DNSP charges for its services should reflect the DNSP's efficient costs of providing those services to each consumer.



Long run marginal cost

- To send efficient future cost signals to consumers the draft rule requires DNSPs to base network tariffs on the LRMC of providing network services.
- Prices that send future cost signals:
 - allow consumers to make efficient consumption and investment decisions.
 - result in lower average network prices for consumers in the long run.
 - reduce cross subsidies between consumers.
 - provide efficient signals to network businesses in making investment decisions.

Long run marginal cost – factors

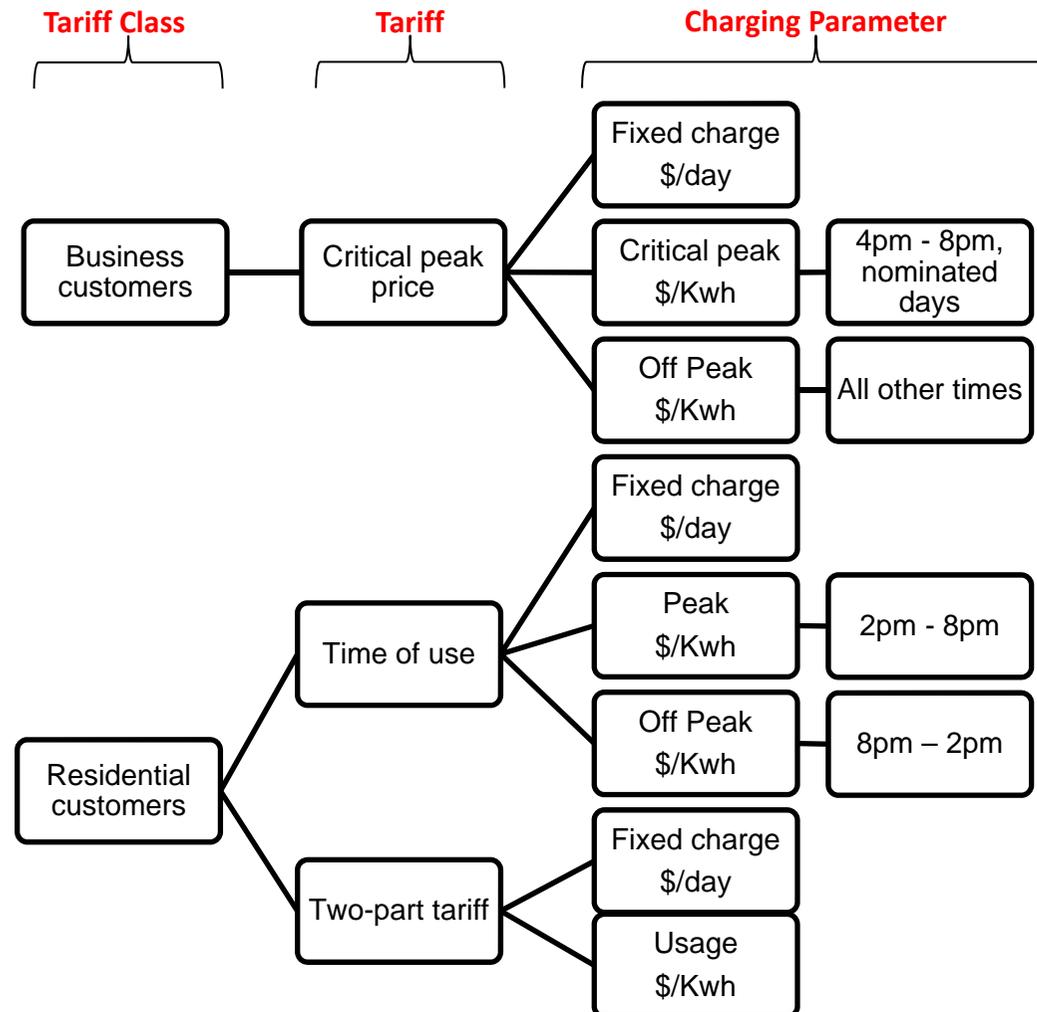
- DNSPs should have the flexibility to implement LRMC based network prices in the way that best suits their network characteristics. The draft rule does this by not specifying the method for calculating LRMC.
- Factors that DNSPs must take into account in calculating and applying LRMC:
 - the costs and benefits associated with using and applying that method;
 - the extent to which consumers are able to receive and respond to price signals;
 - the additional costs likely to be associated with meeting demand from the relevant consumers at times of greatest utilisation of the relevant part of the distribution network; and
 - the location of the relevant consumers and the extent to which costs vary between different locations in the distribution network.

Total efficient cost recovery

The total revenue expected to be recovered from all consumers must permit the DNSP to recover its expected revenue as determined in accordance with the AER's distribution determination.

The revenue recovered from each tariff should reflect the efficient costs of providing network services to the consumers assigned to each tariff.

DNSPs must recover their revenues in a way that minimises distortions to the price signals for efficient usage that would be sent by LRMC based prices.



Consumer Impact Principle

- The draft rule introduces a consumer impact principle to support the network pricing objective. The principle is comprised of two parts, requiring:
 1. DNSPs to set network prices that consumers are reasonably capable of understanding.
 2. DNSPs to minimise the impacts of network price changes on consumers.
- The draft rule allows DNSPs to depart from cost reflective prices to the extent necessary to meet this consumer impact principle. DNSPs will be required to transparently explain how they have done so.
- DNSPs can gradually transition to more cost reflective network tariffs over time to manage these impacts.

Jurisdictional Pricing Obligation Principle

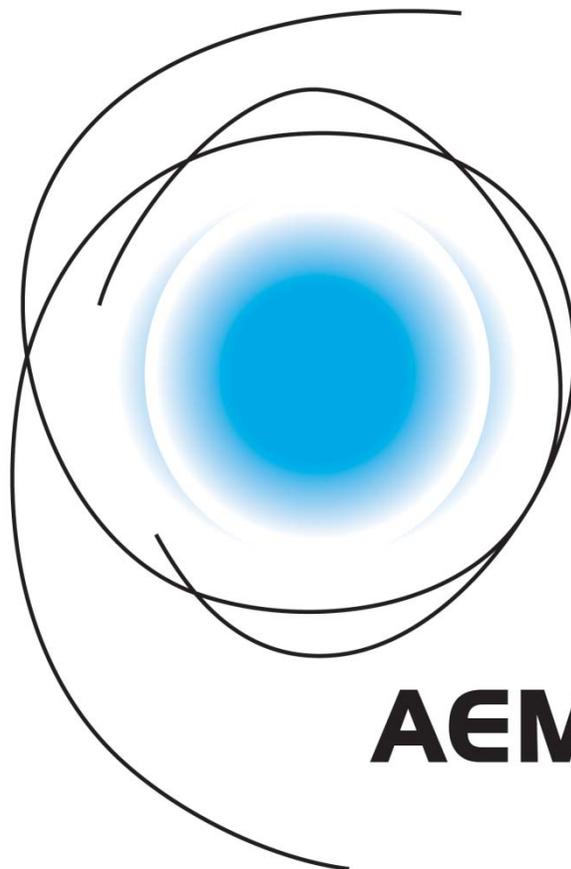
- DNSPs have network pricing requirements placed on them through jurisdictional obligations e.g. several states have uniform state-wide network pricing obligations.
- A requirement to set network prices to meet the network pricing objective and the pricing principles for cost reflectivity could create a conflict with jurisdictional pricing obligations.
- To allow DNSPs to meet the pricing principles and jurisdictional pricing obligations the draft rule introduces a jurisdictional pricing obligation principle which allows DNSPs to depart from cost reflective prices to the minimum extent necessary to meet jurisdictional pricing obligations.

Minor changes: Side constraints, tariff classes and stand-alone and avoidable cost bounds

- Side constraints – the draft rule:
 - removes the ambiguity to provide that side constraints apply equally to all consumers.
 - does not extend the application of side constraints across regulatory periods.
- The draft rule retains the tariff class provisions.
- The draft rule retains the stand-alone and avoidable cost bounds for tariff classes.

Comparison of current and draft principles

	Existing principle	New principle
Network pricing objective	No current objective	Each network tariff should reflect the efficient cost of providing network services to the consumers assigned to the tariff.
LRMC	Take into account LRMC	Network tariffs must be based on the LRMC of providing network services.
Total efficient cost recovery	Recovered with minimum distortion to efficient patterns of consumption	<ol style="list-style-type: none"> 1. DNSPs allowed to recover the expected revenue determined by the AER. 2. Each tariff must recover the total efficient costs of serving the consumers assigned to that tariff. 3. Minimum distortions to the price signals for efficient usage provided by LRMC based prices.
Consumer impact	No current principle	<ol style="list-style-type: none"> 1. Network tariffs which consumers are reasonably capable of understanding. 2. Minimise the impact of tariff changes on consumers.
Jurisdictional pricing obligation	No current principle	DNSPs may depart from network tariffs that meet the above principles to the minimum extent necessary to meet jurisdictional pricing obligations.



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