INFORMATION

# New rules for distribution network pricing

## Publication of final determination and final rule

**The AEMC has made a final rule that requires network prices to reflect the efficient cost of providing network services to individual consumers so that they can make more informed decisions about their electricity usage.**

### What did we decide in the final determination?

In the final determination, we have set a new pricing objective for distribution businesses so prices reflect the efficient costs of providing network services to each consumer. This will allow consumers to compare the value they place on using the network with the costs of using it.

The distribution businesses must comply with four new pricing principles to achieve this objective:

- Each network tariff must be based on the long run marginal cost of providing the service. If consumers choose to take actions that will reduce future network costs, such as by reducing peak demand, then they will be rewarded with lower network charges. Network businesses will have flexibility about how they measure long run marginal cost.
- The revenue to be recovered from each network tariff must recover the network business' total efficient costs of providing services in a way that minimises distortions to price signals that encourage efficient use of the network by consumers.
- Tariffs are to be developed in line with a new consumer impact principle that requires network businesses to consider the impact on consumers of changes in network prices and develop price structures that are able to be understood by consumers. Consumers are more likely to be able to respond to the price signals that network prices are designed to send if they can relate their usage decisions to network price structures and sudden price changes are avoided. Network businesses can gradually phase-in new price structures.
- Network tariffs must comply with any jurisdictional pricing obligations imposed by state or territory governments. But if network businesses need to depart from the above principles to meet jurisdictional pricing obligations, they must do so transparently and only to the minimum extent necessary.

The final rule also retains the existing pricing principle that is designed to avoid cross-subsidies between different classes of consumers, for example residential and business consumers. This principle requires the level of network prices for a tariff class to be between the avoidable cost of not providing the service and the stand-alone cost of providing the service to the relevant consumers. The existing side constraints, which limit annual price movements within a tariff class, are also retained.

The final rule and determination also clarify how the pricing objective and principles work together.

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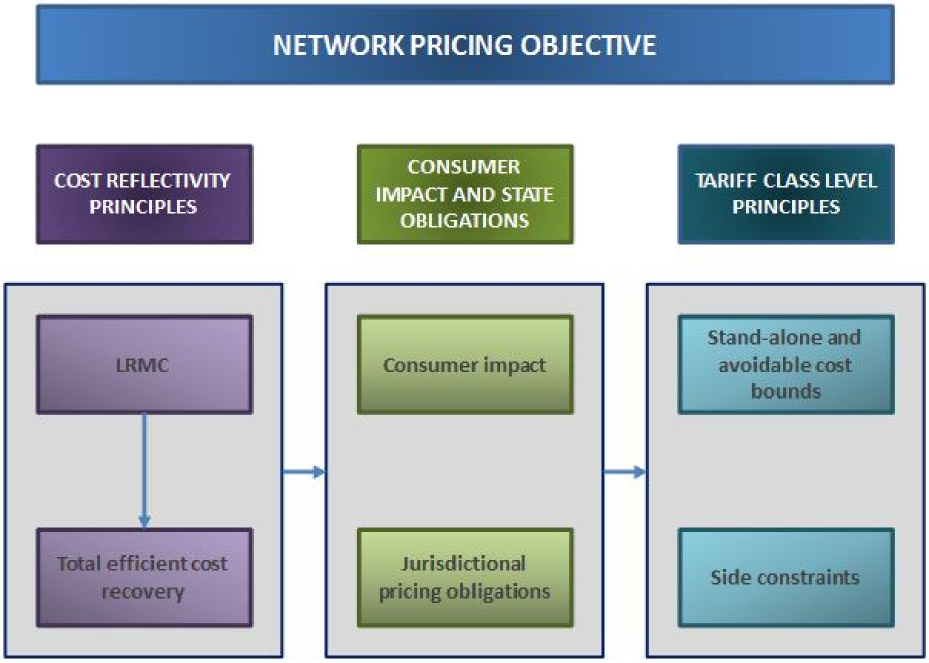
This change puts consumers at the centre of future decision-making about energy.

It means the prices we pay will reflect the actual costs of providing electricity at different times.

Network businesses must comply with the principles in a way that contributes to the objective. If there is a conflict between the principles, the final rule specifies the order of priority of the principles and the extent of businesses' ability to depart from one of the principles to resolve that conflict.

The relationship between the pricing objective and pricing principles is summarised in the following diagram.




## How will the change impact the way prices are set?

The final rule contains a new process and new timeframes for setting network prices to improve certainty, timeliness and transparency for consumers and retailers.

Distribution businesses will be required to:

- Develop a tariff structure statement for approval by the AER as part of their five-year regulatory reset process. The price structures to apply for the regulatory period will be approved as part of this process. Price levels will continue to be approved annually, but an indicative pricing schedule will give consumers and retailers more information about likely price levels over the regulatory period.
- Demonstrate to the AER how they have consulted with consumers and retailers in developing their price structures.
- Notify consumers and retailers of final network prices at least six weeks before they commence, allowing them to better prepare for price changes.

## When do the final rules commence?

Network prices, based on the new pricing objective and pricing principles will start no later than 2017.

Network businesses will shortly need to commence consulting with retailers and consumers on the network prices that they propose to apply from 2017. Under the final rule, network businesses will need to submit their initial tariff structure statement to the AER by late 2015.

## Building on the 2012 network regulation reforms

These changes form part of the ongoing reform of network regulation, which includes significant rule changes made in November 2012 to better equip the regulator to set efficient revenues for network businesses.

This final determination does not change the rules regarding how much revenue network businesses may earn in total. Instead, it is the next step in the reform process and relates to how network businesses divide up that total amount of revenue into network prices that apply to individual consumers.

**New prices are likely to be phased in from 2017 but the rules allow for a gradual transition to avoid price shocks.**

## AEMC Power of Choice Reform Program

This rule change is the second rule change completed as part of a reform program identified by the 2012 AEMC Power of Choice Review to help consumers participate more effectively in energy markets. The first rule change addressed the regulations that allow customers access to information about their energy consumption.

The AEMC is currently assessing a series of other Power of Choice rule changes: expanding competition in metering and related services; AEMO obtaining better demand side participation information; and reform of the demand management embedded generation incentive scheme.

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