



Advice on a Best Practice Retail Price Regulation Methodology

Publication of issues paper

The AEMC has been requested to provide advice on a best practice method for setting regulated retail electricity prices for small customers. The AEMC has published an issues paper for public consultation to commence the first stage of this work.

Purpose of the review

Most small electricity customers can choose to be supplied under a standard electricity contract or under a competitive market offer. In all states and territories, except for Victoria and South Australia, the price of standard electricity contracts is set by a jurisdictional regulator or government. The price of market offers is set by retailers.

The approach taken to setting the regulated standard contract price for small customers currently differs from jurisdiction to jurisdiction. Decisions about the retention of retail price regulation and how prices are regulated are made by jurisdictional governments.

The AEMC has been requested to provide this advice by the Standing Council on Energy and Resources (SCER) as part of a broader package of energy market reforms agreed to by the Council of Australian Governments (CoAG) in late 2012. In providing this advice, the AEMC has been asked to develop a best practice method for setting regulated retail electricity prices for small customers.

CoAG and SCER are committed to deregulating retail prices, where competition is effective. Therefore, the AEMC's best practice method will seek to facilitate the development of competition in retail markets, where this may be feasible.

The AEMC's approach to the review

A stable, clear and coherent objective is key to effective retail price regulation. Once this has been established, the objective can assist regulators and governments in making decisions in relation to how retail prices should be regulated.

The AEMC has articulated a proposed objective, and principles for setting regulated retail prices in our issues paper for comment.

We will identify the different methods for setting regulated retail prices, and assess these methods against the objectives and principles. This analysis will then form the basis of the AEMC's final advice.

Issues for stakeholder comment

Proposed objective and principles for retail price regulation

The AEMC's proposed objective for retail price regulation seeks to accommodate the differing retail markets that are in place across the jurisdictions.

It balances the need for regulated retail prices to reflect the efficient costs of providing electricity services and the longer term need to facilitate the development of competition, where this may be feasible.

This objective will be supported by a number of principles, which will be used to guide the assessment and development of our best practice method.

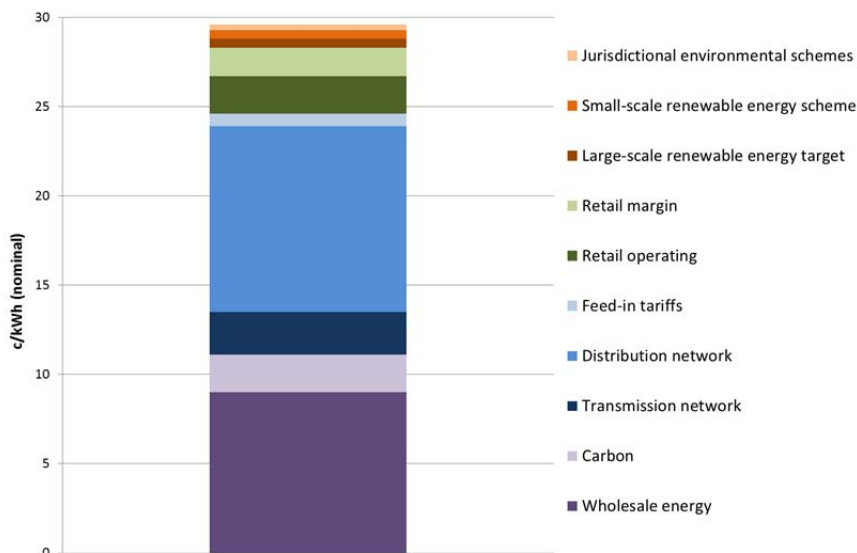
Submissions on the issues paper are due by 12 July 2013.

Key cost components

Retailers face a range of different costs in providing electricity services to customers. Jurisdictional regulators set the price of standard electricity contracts by estimating each cost component that is likely to be faced by the retailer.

Together these cost components comprise the retail cost stack, which is used to set the regulated retail price. An indicative residential retail price stack is illustrated below.

National – residential retail price cost stack (2012/13)



Jurisdictional regulators do not have a formal role in setting each cost component of the retail price stack. For example, transmission and distribution network costs, which comprise significant components of the retail price stack, are set under a separate process by the Australian Energy Regulator (AER). Jurisdictional regulators simply include the network costs as part of the retail cost stack in setting the regulated retail price.

However, for the remaining cost components, the jurisdictional regulator does have a formal role in setting these components. For example, in setting the wholesale energy cost component, jurisdictional regulators seek to estimate the costs to the retailer of purchasing electricity through the wholesale market.

Some of the cost components can present particular cost recovery risks for retailers, which may affect their willingness to enter retail markets. This in turn has implications for the level of competition and choice customers have in determining how their electricity is supplied.

The AEMC considers that the key components of the retail price stack include: wholesale energy costs; retail margins; and environmental scheme costs. As a result, the AEMC is particularly interested in stakeholder views in relation to the most appropriate method for setting these cost components.

Next steps

Submissions on the issues paper close on 12 July 2013.

As required by SCER's terms of reference, following the consideration of written submissions and issues raised by stakeholders, the AEMC will provide a draft report to jurisdictions and jurisdictional regulators for comment by 30 August 2013.

A final report setting out our advice on a best practice method or methods for retail price regulation will then be published by 30 September 2013.

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