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CLEAN ENERGY COUNCIL

19 December 2013

John Pierce, Chairman
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235
By Email

Dear Mr Pierce,

RE: Clean Energy Council Submission to ERC0161 National Electricity Arrangement (Distribution Network Pricing Arrangements) Rule 2014

The Clean Energy Council (CEC) welcomes the opportunity to provide comment on the Australian Energy Market Commission's Consultation Paper on the proposed Rule Change ERC0161.

The CEC is the peak body representing Australia's clean energy and energy efficiency industries. Its priorities are to:

- create the optimal conditions in Australia to stimulate investment in the development and deployment of world's best clean energy technologies
- develop effective legislation and regulation to improve energy efficiency
- work to reduce costs and remove all other barriers to accessing clean energy

The CEC works with over 550 member organisations and governments to identify and address the barriers to efficient industry development in the energy efficiency and stationary energy sector. The clean energy industry contributes to the generation of electricity using wind, hydro, solar, biomass, geothermal and marine energy as well as the emerging technologies and service providers in the energy efficiency sector including solar hot water and cogeneration.

The CEC provides the following high level responses to the questions posed by the Consultation Paper. These responses are outlined in greater detail in the attached submission.

- It is crucial that consumers are able to respond to price signals. Consumers are unable to respond to an increase in fixed charges, other than to disconnect from the grid. It would be undesirable to send price signals that encourage disconnection. We therefore strongly emphasise the undesirability of any moves toward a greater fixed charge component for electricity tariffs.

- The Australian Energy Regulator (AER) needs more oversight of how tariffs are structured. We welcome the proposal to subject Pricing Structure Statements to review by the AER.

- We also welcome the proposal to clarify that the 'side constraint' provisions on tariff price changes should apply regardless of whether consumers have interval meters or traditional accumulation meters.

- In addition to the information proposed by the Standing Council on Energy and Resources (SCER), a network tariff structures document should include an explanation of the triggers that cause a customer to be moved from one tariff class to another.

- The AER should be required to develop binding guidelines for consultation by DNSPs.

- The pricing structures statement process should be introduced as soon as possible. The AER consultation guideline should ideally be in in place before the PSS process is fully implemented. To enable this in time for the next regulatory process, this rule change should be fast-tracked. The AER should be instructed to commence development of indicative guidelines to assist DNSPs whose regulatory proposals are due in 2014.

In closing the CEC would like to reiterate the view that this rule change is a very important step in improving predictability, stakeholder engagement and allocation of risks in the tariff setting process for DNSPs.

Please do not hesitate to contact the undersigned for any queries regarding this submission.

Yours sincerely,

Darren Gladman
Policy Manager

CEC submission to AEMC Consultation Paper on ERC0161: National Electricity Amendment (Distribution Network Pricing Arrangements) Rule 2014

Executive Summary

The Clean Energy Council (CEC) welcomes the objectives of the rule change and the approach to its decisions proposed by the Australian Energy Market Commission (AEMC), as summarised in the Executive Summary of the Consultation Paper. We welcome moves to improve the opportunity for those affected by distribution network prices to be consulted on the development of those prices. Furthermore, we welcome the AEMC's commitment to follow a technology neutral approach to its decisions and to affirm the principle that consumers should be able to respond to the price signals arising from distribution network tariffs.

The Australian Energy Regulator (AER) needs more oversight of how tariffs are structured. We welcome the proposal to strengthen the role of the AER in approving network charges and charging structures by requiring distribution businesses to publish a Pricing Structure Statement (PSS) and to subject each PSS to review by the AER.

We support PSS proposal put forward by the Standing Council on Energy and Resources (SCER) and in addition we would welcome greater transparency on the rules as they relate to triggers that a DNSP can use to shift a customer from one tariff structure to another. CEC would support either of the following approaches:

1 An annual PSS setting tariff structures *and* levels, subject to consultation and AER approval and with a requirement for the Distribution Network Service Provider (DNSP) to demonstrate how they have taken account of the consultation in their application for approval of the annual PSS; or

2 A 5-yearly determination setting tariff structures, and an annual PSS setting price levels, subject to consultation and AER approval and with a requirement on DNSPs to demonstrate how the structures meet the pricing principles, adherence to the approved structures and how consultation has been taken into account. The annual process should also consult on the effectiveness/impacts of the structures. This collective feedback should then feed into the level setting in next annual PSS and the structure setting in the next determination.

Either approach would increase accountability to AER, increase consumer engagement, codify pricing principles and demonstrate compliance with these principles. Either approach should also involve an AER-produced guideline for DSNP's PSS documents and approval by the AER on both levels and structures.

We also welcome the proposal to clarify that the 'side constraint' provisions on tariff price changes should apply regardless of whether consumers have interval meters or traditional accumulation meters. It would be unfair to discriminate against consumers with interval meters, particularly since governments have actively encouraged consumers to adopt interval meters.

Response to Questions in Consultation Paper

1. ***What other considerations should be included in the assessment framework?***

The Clean Energy Council (CEC) supports fair and efficient pricing for electricity. We agree that electricity pricing is crucial to influencing demand on the network. The considerations included in the assessment framework appear to be appropriate. Consideration of the allocation of risks raises issues related to changes in technology and falling demand. These issues were addressed in a report recently released by the Grattan Institute[1], which notes that governments will need to decide who should pay for the reduction in the value of distribution networks brought about by changes in technology and electricity demand.

We would like to emphasise the importance of ensuring that consumers are able to respond to price signals. Consumers are unable to respond to an increase in fixed charges, other than to disconnect from the grid. It would be undesirable to send price signals that encourage disconnection. We therefore strongly emphasise the undesirability of any moves toward a greater fixed charge component for electricity tariffs. Fixed charges are potentially the most regressive because they do not allow for cost minimisation through behaviour change. Demand or capacity charges are preferable to fixed charges. A demand or capacity charge may go some way to addressing cross subsidies between customers with and without air conditioning.

3. ***How often are the tariff structures likely to change during a regulatory period and what are some of the reasons for that change?***

From the customer perspective, a change in network tariff structure can be triggered by installation of solar PV systems. This is a matter of significant concern. A recent information sheet issued by SA Power Networks describes a business whose electricity bill increased from about $19,000 per annum to about $30,000 per annum following the installation of a solar PV array. This is a clear and extreme financial disincentive to the installation of solar PV and represents a significant barrier to the adoption of solar PV systems by some South Australian businesses.

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?***

In addition to the information proposed by SCER, a network tariff structures document should include an explanation of the triggers that cause a customer to be moved from one tariff class to another.

[1] Wood, T. and Carter, L. 2013. Shock to the system: Dealing with falling electricity demand. Grattan Institute

A key concern for the solar PV industry is that the installation of a rooftop solar PV system is often accompanied by a change in metering or switchboard configuration. Changes in metering and switchboard configurations can trigger changes in a customer's tariff structure. For example, there have been reported a number of cases of customers who install solar PV and are subsequently shifted from a tariff dominated by volumetric charges to one dominated by demand charges. This would appear to contravene the spirit, if not the letter of clause 6.18.4(a)(3) of the National Electricity Rules, which require that:

> "customers with micro-generation facilities should be treated no less favourably than customers without such facilities but with a similar load profile"

It is unclear whether the AER has the authority to intervene to address this concern. The situation would benefit from greater transparency and clarification of the rules regarding tariff changes that are, in effect, triggered by the installation of solar PV. The limited control of the AER within the current arrangements is probably not consistent with the firmly held desire to encourage consumer participation in the market. The ability of SA Power Networks to switch customers to a demand tariff following installation of solar PV demonstrates this.

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

Figure 6.2 is missing an option. Structures could be approved in the 5 year determination, with pricing levels consulted and approved annually in the PSS. This would overcome the risk to the revenues of DNSPs.

DNSPs should not be permitted to vary their network tariff structures within the regulatory period. Allowing them to do so would devalue the consultation process and provide no additional certainty compared with the current situation.

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?***

An 'indicative' document would be of limited value, in terms of improving transparency, customer engagement and predictability. DNSPs should be required to apply the document in their annual pricing proposals and demonstrate compliance.

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?***

Changes should be either approved annually or within the determination. There should be no changes within the annual network pricing process.

If they are to occur, variations should be approved by the AER and demonstrate consistency with AER guidelines for changes, which would need to be developed.

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. Anything less has potential to undermine efforts to improve customer engagement.

9. ***Is consultation necessary if DNSPs seek to amend their approved pricing structures statement during the regulatory period, as opposed to at the time of the regulatory determination? Are there any circumstances where amendments to the network tariff structures in the annual pricing process should be exempt from consultation on amendments to the previously approved pricing structure statement?***

Yes, there should be a requirement for consultation whenever a DNSP seeks to amend their pricing structure statement. There should not be any circumstances where amendments to the tariff structures are exempt from consultation.

10. ***Is it necessary for the AER (as opposed to the DNSP) to consult with stakeholders before approving any proposed amendments to the pricing structure statement sought by the DNSP?***

Yes. It would be preferable if amendments to the pricing structure statement were limited to an annual review process, with no further amendments allowed between reviews.

Both the DNSP and the AER should consult with stakeholders during the course of the annual review process.

Ultimately, the onus should be on the AER to make decisions in the best interests of consumers. The PSS and tariff setting processes should be exempt from the Merits Review process.

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

The AER should be required to develop binding guidelines for consultation by DNSPs. In the absence of the discipline of a competitive market, there is a need for regulation to ensure adequate consumer consultation by regulated monopoly businesses such as DNSPs.

12. ***Does the PSS need to be approved?***

Yes. The PSS should be subject to approval by the AER in accordance with AER guidelines. Approval should require demonstrating that pricing principles and other relevant criteria have been satisfied.

13. ***Should the AER be able to amend a DNSP’s PSS? If the AER does not approve a DNSP’s proposed pricing structures statement, what arrangements would be suitable for default network tariff structures?***

Yes. If the PSS is inconsistent with the AER guidelines then the AER should have the option of amending the PSS or allowing tariffs to default to the most recent year’s annual pricing proposal.

14. ***What are the risks to the annual pricing process if DNSPs do not comply with their approved pricing structures statement or are late submitting a full pricing proposal?***

Risks will be minimised if the AER guidelines are completed and the AER has the option of amending the PSS or allowing tariffs to default to the most recent year's annual pricing proposal. Annual level setting would further assist in addressing this risk.

15. ***How should the DNSPs be incentivised to comply with their approved pricing structure statement in their annual pricing proposals? How should compliance incentives be balanced against the financial risks for DNSPs and certainty for stakeholders?***

Compliance incentives must involve a degree of financial risk. Otherwise, where is the incentive to comply? It will be the role of the DNSP to manage this risk. Clear AER guidelines and expectations will assist in managing this risk.

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

Yes. DNSPs currently forecast expenditure five years ahead in their resets, so it is not unreasonable to require them to forecast the costs their customers will face too. They should also be made to demonstrate reasons for a divergence from a forecast in the PSS approval process.

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. There should be an annual consultation process for any proposed changes to levels and structures.

18. ***Should a pricing structures statement process be introduced as soon as possible? If so, what risks are there from having it in place before the next regulatory determination period?***

Yes, the PSS process should be introduced as soon as possible.

There is time to introduce the PSS process in time for the next regulatory determination process, albeit with a curtailed process of consultation initially. The AER should be instructed to expedite the development of the necessary guidelines as a matter of urgency.

19. ***Does the AER consultation guideline need to be in place before a PSS can be implemented?***

Yes. This rule change should be fast-tracked to enable the process. The AER should be instructed to commence development of indicative guidelines to assist DNSPs whose regulatory proposals are due in 2014.

21. ***What would be the likely impacts on customers of making an LRMC approach mandatory?***

From an economic perspective LRMC is a logical approach and should result in a long term reduction in network costs for all customers, assuming that this price signal is passed through by retailers and their customers are willing and able to respond rationally. However, the approach may seem inequitable. For example, rural customers might be required to pay steep increases in network fees in some areas. There would also be financial advantages for customers in areas where the network has recently been augmented and disadvantages for customers in areas that are due for augmentation soon. There may need to be some degree of smearing (at least in the initial phase) to overcome perceptions of inequity and consumer resistance.

22. ***What would be the impacts on DNSPs of making an LRMC approach mandatory? Does it result in increased compliance risk?***

As noted in the Consultation Paper, a requirement to make the use of the LRMC approach mandatory is likely to facilitate more widespread use of time-based and locational pricing.

Guidance may be required in the way that DNSPs can smear tariffs in order to meet the dual objectives of using the LRMC approach while taking into account the impact on customers of changes to network tariffs.

24. ***Should LRMC be defined? If so, what level of detail would be appropriate?***

Yes. LRMC should be defined in AER guidelines and possibly the National Electricity Rules.

25. ***Should one methodology apply to calculating LRMC or should multiple methodologies be allowed? Which is/are the most appropriate methodology(ies)?***

Allowing DNSPs to develop their own methodologies for LRMC would risk ‘gaming’ of the system. To allow some initial flexibility it may be appropriate to specify the preferred methodology in an AER guideline with a provision for variation. All methodologies should be subject to approval by AER. If a DNSP wishes to deviate from a standard LRMC approach they should at least be required to publish estimates under the standard approach and the approach proposed in the DNSP’s variation. Proposals to vary LRMC methodology should be subject to consultation.

26. ***Should the AER be required through a guideline to specify the methodology or methodologies of calculating and applying LRMC?***

The AER should be required to publish guidelines on a preferred methodology for calculating LRMC. A DNSP that wishes to deviate from the preferred LRMC methodology should at least be required to publish estimates under the standard approach and the approach proposed in the DNSP’s variation. Proposals to vary LRMC methodology should be subject to consultation.

28. ***How should LRMC pricing reflect additional costs associated with coincident peak demand and what are the practical impediments to DNSPs adopting tariffs that reflect coincident peak demand?***

The economic logic would appear to dictate the use of critical peak pricing, assuming that the applicable metering is available. Where consumers are charged cost-reflective tariffs at critical peak periods there should also be provision for payment of benefit-reflective feed-in tariffs that provide a financial incentive for distributed generation and storage to play a role in reducing network augmentation requirements. By spreading the electricity load more evenly to improve network utilisation and manage growth in peak demand, spending of millions of dollars on asset augmentation can be avoided. Ultimately, all consumers will benefit from moves to align tariffs with the high cost of supplying electricity to meet peak demand, while rewarding customers who shift consumption to times of low usage. Economic benefits will be even greater if distributed generators see financial incentives to increase supply at critical peak periods.

29. ***How important are locational pricing signals for distribution networks? Are locational pricing signals for some types of customers more important than others?***

The economic logic underlying the SCER proposal implies a shift to location-specific distribution tariffs. The need for network augmentation is location-specific. If tariffs are intended to send price signals that alter consumption in a way that reduces the need for future investment in network augmentation then distribution tariffs should be location-specific.

As noted above, there may be perceptions of inequity associated with a move toward location-specific distribution tariffs.

Application of cost-reflective, location-specific distribution tariffs should commence with larger electricity consumers, with residential customers a lower order priority for this reform.

30. ***What are the practical impediments to DNSPs adopting tariffs that reflect locational pricing signals?***

Political considerations are likely to be the most significant barrier to the adoption of locational pricing signals by DNSPs.

31. ***Is an additional principle required to further encourage network prices which are based on the drivers of network costs to the maximum extent possible?***

It is not immediately apparent whether an additional principle is required to encourage network prices to be based on drivers of network costs. Further information would assist in responding to this question. Beyond LRMC, what other measures would be a useful proxy for quantifying the drivers of network costs?

32. What are the pros and cons of using a Ramsey pricing approach or a postage stamp pricing approach?

The postage stamp approach is fairer than the Ramsey pricing approach. Shifting costs to consumers with the lowest price responsiveness runs counter to the principle of having regard to whether a consumer is able or likely to respond to price signals.

Whichever approach AEMC chooses to support, the decision must be backed by evidence that it would reasonably reflect the magnitude and distribution of the residual network costs of the relevant DNSP.

37. Should a requirement for DNSPs to take into account the impact of tariffs on consumers be included in the pricing principles?

Yes.

38. If a requirement is included, does the proposed principle provide enough guidance on how it is to be complied with, or would an AER guideline be useful?

An AER guideline would be useful.

40. Should network tariffs reflect transmission pricing signals? If so, what would be the most appropriate way to achieve this for different types of network customers?

Transmission investment is not as easily allocated to a group of users as distribution because it tends to be over-built to meet large divergences in power flows and in both directions. In many cases multiple DNSPs benefit from investment in transmission, rather than more easily identified distribution customers. In any case it forms a relatively small portion of the network charges.

43. Is the proposal to apply side constraints across regulatory periods likely to materially benefit consumers by protecting them from price shocks?

The merits of the proposal are unclear. Further consideration of the costs and benefits of the proposal is warranted. As noted in the Consultation Paper, the proposed requirement for DNSPs to take consumer impacts into account may reduce the need to apply side constraints across regulatory periods.

46. Should network tariffs of customers with interval meters or other types of time-based meters be subject to side constraints?

Customers should be treated consistently, irrespective of the meter technology they use. This is a matter of significant concern for the solar PV industry. From the customer perspective, a change in network tariff structure can be triggered by installation of solar PV systems if that is associated with a meter change. This is unfair and is a disincentive to the adoption of advanced metering and distributed generation and storage. It represents a significant barrier to the adoption of solar PV systems, especially by some adversely affected businesses (eg. in South Australia).

Customers with interval meters should be subject to side constraints to the same extent as customers without an interval meter (and assuming a similar load profile).