

## **1 INTRODUCTION**

### **1.1 PURPOSE OF THIS SUBMISSION**

ENERGEX provides this submission in response to *the Review of the Electricity Transmission Revenue and Pricing Scoping Paper* (Scoping Paper) released by the Australian Energy Market Commission (the Commission) in July 2005.

The Commission is required to undertake a review of the National Electricity Rules (the Rules) for electricity transmission revenue and price regulation (the Review). The purpose of the Scoping Paper is to seek stakeholder comments on the scope of the Review and the key issues it needs to address.

This submission seeks to address each of the items raised by the Commission in the Scoping Paper. Other matters not included in the Scoping Paper but considered important by ENERGEX are also outlined in this submission.

It is a joint submission made by ENERGEX Limited and ENERGEX Retail Pty Ltd. The name ENERGEX will be used throughout this paper as a reference to this group.

### **1.2 OVERVIEW OF THE SUBMISSION**

The submission is structured in accordance with the Scoping Paper. That is, it addresses each of the Commission's questions under the following sections:

- Section 2: National Electricity Law requirements;
- Section 3: Issues relevant to the development of electricity transmission revenue and pricing Rules;
- Section 4: Economic regulation of electricity transmission revenue;
- Section 5: Economic regulation of electricity transmission prices; and
- Section 6: Regulatory discretion and procedural requirements.

### **1.3 KEY ISSUES**

The main issues for ENERGEX are as follows:

- ENERGEX agrees that while there is similarity between electricity transmission and distribution operations, regulation needs to be cognisant of some specific differences that exist between the networks particularly in regard to pricing;
- While ENERGEX believes that alternative approaches to the CPI-X building block should be assessed, such consideration of further changes at this time should be balanced with the provision of regulatory certainty;
- ENERGEX submits that this Review should consider the range and structure of charges to ensure that they provide the appropriate price signals to network users and generators;
- ENERGEX is concerned that the Review proceeds in a timely fashion given the Commission's proposed two-stage approach; and
- ENERGEX submits that the procedural requirements should reflect current policy "best practice" and also allow for a merits review of the regulator's decision.

## 2 NATIONAL ELECTRICITY LAW REQUIREMENTS

### 2.1 TRANSITIONAL ARRANGEMENTS

***The Commission invites comment on the inclusion of any issues that may relate to savings and transitional arrangements.***

While ENERGEX believes that any changes that result in more efficient revenue regulation and network pricing should be implemented as soon as possible, ENERGEX also recognises that it is not appropriate to re-open an existing revenue determination solely on the basis of inconsistencies with any new or amended Rules resulting from this Review.

For regulatory certainty, existing determinations should remain in force for the expected duration of the current regulatory periods for each of the transmission companies, and transitional arrangements will be needed to ensure effective management to any new Rules.

## 3 ISSUES RELEVANT TO THE DEVELOPMENT OF ELECTRICITY TRANSMISSION REVENUE AND PRICING RULES

### 3.1 CHAPTER 5 ISSUES

***The Commission invites comment on the relevance of each of these Rules to this Review and whether there are other Rules which are beyond the scope of this review but which may be relevant to it.***

ENERGEX believes that a review of the Rules contained in Chapter 5 are beyond the scope of this Review. However, the Chapter 5 issues identified by the Commission are fundamentally linked to the issues of revenue and price regulation, and will need to be taken into consideration in developing any new Chapter 6 Rules as part of the current Review.

In regards to the Regulatory Test specifically, ENERGEX understands that the Ministerial Council on Energy (MCE) will submit revised Regulatory Test Principles as MCE-initiated Rule changes for consideration by the Commission.<sup>1</sup> These principles will provide guidance to the AER in applying the Regulatory Test. Given the MCE's intentions, a separate review of the Regulatory Test by the Commission may not be appropriate at this time.

In addition, ENERGEX believes it is also important to take into consideration the work undertaken on regional boundaries. The MCE has indicated that MCE-initiated Rule changes on Regional Boundary Structure and Change Criteria will also be submitted to the AEMC.<sup>2</sup>

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<sup>1</sup> Ministerial Council on Energy, *Statement on NEM Electricity Transmission*, May 2005, p.2.

<sup>2</sup> Ministerial Council on Energy, *Statement on NEM Electricity Transmission*, May 2005, p.7.

### 3.2 MARKET NETWORK SERVICE PROVIDERS (MNSP)

***The Commission invites comment on whether, and to what extent the Rules that provide for non-regulated transmission systems may be relevant to specific matters in this Review.***

ENERGEX believes the Rules for non-regulated transmission systems are outside the scope of this Review.

ENERGEX notes that the ACCC, as part of the development of a revised Regulatory Test, removed the existing biases against the regulated transmission investments.<sup>3</sup> ENERGEX submits that any consideration of the Rules relating to non-regulated transmission systems, to the extent that they are within the scope of this Review, should have regard to the work undertaken in the Regulatory Test on this issue.

## 4 ECONOMIC REGULATION OF ELECTRICITY TRANSMISSION REVENUE

### 4.1 FORM OF REGULATION

***The Commission invites comment on whether, in the light of the NEM objective and the requirements of s.35(3), this Review should consider alternative approaches to the current CPI-X building block approach.***

ENERGEX believes that this Review should consider and test all alternative approaches to the current CPI-X building block approach.

While ENERGEX's view is that the National Electricity Law does not prevent the Development of Rules that provide flexibility to adopt alternative forms of regulation, any adoption of an alternate approach needs to recognise that network companies require certainty when making long term investments.

### 4.2 MECHANISM FOR ESTABLISHING THE REVENUE REQUIREMENT

#### 4.2.1 Asset Base and Criteria for Determining Efficient Investment

***The Commission invites comment as to whether there are any other issues that need to be considered in this Review in addition to those identified above.***

ENERGEX agrees that the issues highlighted by the Commission in its Scoping Paper need to be considered in this Review. In addition, ENERGEX believes the Commission should also consider the most appropriate approach to the roll-forward of the asset base.

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<sup>3</sup> Ministerial Council on Energy, *Statement on NEM Electricity Transmission*, May 2005, p.2.

#### 4.2.2 Depreciation, Return on Investment and Operating Expenditure

***The Commission invites comment on whether there are costs additional to those outlined above that should be considered as part of the Review.***

ENERGEX agrees that the matters highlighted by the Commission in its Scoping Paper, including the need for a pass-through mechanism, need to be considered in this Review.

ENERGEX submits that the Review should also consider the following costs:

- Working capital;
- Self-insurance; and
- Tax (where a post-tax framework is adopted).

ENERGEX submits that another important issue for consideration in this Review is the transparency of costs that are included in the building block formula (where this is the approach adopted).

#### 4.2.3 Incentive Mechanisms

***The Commission invites comment on what issues should be included when considering incentives for regulated transmission systems to make efficient operating and investment decisions.***

ENERGEX notes that, under the current regulatory framework, there are two elements to the incentive scheme – one being the incentive to out-perform the cost forecasts included in the revenue determination (i.e. efficiency gains above those included in the determination), and the other being the incentive scheme to meet certain service standards. The latter also pertains to the operation of the transmission system in a manner that minimises disruptions to the market.

ENERGEX submits that the following issues need to be considered by the Commission in the development of an incentive mechanism for efficiency gains:

- Relative sharing of efficiency gains between the transmission company and customers / users; and
- Timeframe over which benefits may be retained by the transmission company.

ENERGEX submits that the following issues need to be considered in the development of a service quality incentive scheme:

- Service standards (behavioural, as well as network performance);
- Cost of meeting given service standards;
- Information requirements and reporting;
- Scale of the financial reward / penalty;
- Financial implications of any penalties applied; and
- Symmetry of the rewards and penalties.

Further, the Commission needs to take into consideration the service quality incentive scheme included in the *Service Standards Guidelines*.<sup>4</sup>

#### 4.2.4 Non-transmission Alternatives

***The Commission invites comment on what issues are relevant when considering non-transmission alternatives as part of this Review.***

Currently, there is little mention of alternatives in the Rules. The only obligation is for the regulator to “have regard to the need to ... create an environment in which generation, energy storage, demand side options and network augmentation options are given due and reasonable consideration”.<sup>5</sup> The Rules in Chapter 6 do little to influence (positively or negatively) the consideration of non-transmission alternatives.

However, consideration of alternatives to transmission is an integral component of the Regulatory Test. ENERGEX submits that the Commission needs to take these requirements into consideration in any review of the Rules.

## 5 ECONOMIC REGULATION OF ELECTRICITY TRANSMISSION PRICES

### 5.1 MATTERS IN EXISTING RULES ON ELECTRICITY TRANSMISSION PRICING

***The Commission invites comment as to whether the Rules appropriately cover the scope of matters that ought to be taken into consideration in this Review, and if not, what additional matters, or fewer matters, should be covered under the Rules.***

ENERGEX submits that the Rules appropriately cover the scope of matters that need to be taken into consideration in this Review. ENERGEX's specific comments on each matter are provided below.

#### 5.1.1 Transmission Pricing Arrangements

***The Commission invites comment on whether it should be seeking to simplify and clarify the transmission pricing objectives and principles in the course of the Review.***

ENERGEX believes that, as a general rule, the Commission should always aim to clarify and simplify the objectives and principles included in the Rules.

ENERGEX notes that the Commission seeks comment on whether it should be seeking to simplify and clarify the transmission pricing objectives and principles. However, it does not ask the question are the objectives of regulation being satisfied by the current approach.

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<sup>4</sup> ACCC, *Statement of Principles for the Regulation of Electricity Transmission Revenues – Service Standards Guidelines*, 12 November 2003.

<sup>5</sup> National Electricity Rules, section 6.2.3(d)(2).

### 5.1.2 Range of Charges

*The Commission invites comment on whether this Review should address the range of charges set out above.*

### 5.1.3 TuoS Rebates

*The Commission invites comment on whether this Review should consider avoided TUoS rebates.*

### 5.1.4 Allocation of Shared Network Costs

*The Commission invites comment on whether this Review should consider the allocation of shared network costs between users of the transmission system.*

### 5.1.5 Form of Shared Network Use of System Charges

*The Commission invites comment on whether this Review should consider the methodology(ies) for determining shared network usage charges.*

### 5.1.6 Structure of Charges

*The Commission invites comment on whether this Review should consider the degree of flexibility retained by transmission system operators to determine the structure of charges, and whether alternative structures should be considered.*

ENERGEX submits that all the issues listed in Sections 5.1.2 through to 5.1.6 should be reviewed to ensure appropriate price signals are being provided. In particular, ENERGEX is keen to ensure that the system and market benefits of providing better price signals to generators and customers are fully considered.

### 5.1.7 Inter-regional TuoS Transfers

*The Commission invites comment on whether this Review should consider interregional TUoS transfers.*

ENERGEX submits that this Review should consider inter-regional TUOS transfers.

## 6 REGULATORY DISCRETION AND PROCEDURAL REQUIREMENTS

### 6.1 GUIDING DISCRETION – ECONOMIC REGULATION OF ELECTRICITY TRANSMISSION

***The Commission invites comment on whether this Review should consider the appropriate balance between discretion and prescription when the AER is making a transmission determination.***

ENERGEX believes that the Review should consider the balance between regulator discretion and prescription, with a view to developing a set of Rules that provide greater certainty and minimise regulatory risk.

### 6.2 GUIDING DISCRETION – ELECTRICITY TRANSMISSION PRICING

***The Commission invites comment on whether this Review should consider the balance between unfettered versus guided discretion and formulaic prescription of charges.***

ENERGEX believes that unfettered discretion dilutes regulatory certainty and therefore introduces regulatory risk. The Review should err on the side of providing greater certainty and minimum regulatory risk. In this regard ENERGEX encourages the Commission to be cautious when providing unfettered discretion.

### 6.3 PROCEDURAL REQUIREMENTS FOR AER DECISION MAKING

***The Commission invites comment on what issues are relevant when considering the process to be followed by the AER in making a transmission determination.***

ENERGEX agrees that the matters listed in the Scoping Paper are relevant.

In addition, ENERGEX submits that the procedural requirements should reflect current policy “best practice” and also allow for a merits review of the regulator’s decision.