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Dear Sir/Madam

Review of the Electricity Transmission Revenue and Pricing Rules – Transmission Pricing: Issues Paper

Queensland Rail (QR) welcomes the opportunity to make this submission on the AEMC's Issues Paper entitled "Review of the Electricity Transmission Revenue and Pricing Rules – Transmission Pricing: Issues Paper" (the Paper). Whilst QR is a large electricity transmission customer, QR's interest stems principally from its desire to see a more efficient TUoS charging structure being implemented. In particular, QR is concerned that the current TUoS charging arrangements potentially impedes economic development in Australia.

QR does not intend to address all of the Commission's questions, rather, the theme of this submission is the need for the regulatory framework to support commercial negotiation between TNSPs and major customers with fall back to appropriate arbitration/dispute resolution where necessary.

QR believes that the floor for the pricing of transmission services should be incremental cost. QR accepts that the nature of the transmission network is such that a degree of standardisation in charging is necessary. However, QR believes that there is scope for greater negotiation in TUoS charging arrangements, at least for major loads, and that TNSPs should have confidence that their revenue base will not be imperilled should they choose to offer a discount to retain a significant load on the network that recovers at least incremental cost.

Of critical concern to QR is the need for the framework to address the current inappropriate TUoS discounting arrangements so as to ensure that they remove the possibility that the inflexible application of transmission pricing will result in the loss of major industrial investment. That is, QR believes it is critical that transmission pricing contains sufficient flexibility to allow incremental cost pricing where doing so is necessary to capture (or retain) major loads to the NEM (and with it, the substantial economic benefits associated with those industries).

This is in contrast to the current arrangements whereby discounts are assessed against the cost of so-called inefficient bypass rather than whether the resulting pricing will at least cover incremental costs associated with servicing the customer and potentially make a positive contribution to common costs, thereby ensuring that remaining customers are better off than absent the new load. Further, TNSPs may not always have appropriate incentives to attract additional load to the network under a revenue cap form of regulation.

The remainder of this submission broadly addresses each of the chapters of the Paper in turn.

Chapter 2 – Requirement for Regulation

QR accepts that a degree of prescriptiveness is required for transmission pricing due to the potentially high transactions costs arising from other arrangements. It is therefore appropriate that prescriptive pricing arrangements apply for the vast majority of customers in the NEM. However, QR believes that there needs to be greater flexibility in charging arrangements for major customers, who are distinguished by their size and their sensitivity to TUoS charges. This issue is elaborated upon below.

QR is concerned that revenue caps are unlikely to be an optimal form of regulation for TNSPs. QR considers that if such a form of regulation is to continue, it is imperative that there is recognition that an unintended consequence of that form of regulation is that there can be a positive disincentive for TNSPs to connect new loads to the network – especially major loads that could bring forward capital expenditure.

Accordingly, if this form of regulation is to continue, mechanisms to incentivise TNSPs should be incorporated into the regulatory framework. This may include the capacity to review revenue caps for major new investment and mechanisms to ensure that the incentive structure created by the form of regulation does not result in socially undesirable outcomes. These mechanisms may include the ability for a transmission customer to apply for dispute resolution in the event that a TNSP refuses to discount where it can be established that a discount is necessary to attract a load to the network.

Chapter 3 – Context and Objectives of the Review

In QR's view, achieving *efficient investment in, and efficient use of, electricity services* for major customers requires a flexibility and willingness to discount TUoS charges – to a point where incremental costs are covered - where those discounts are necessary to attract the affected load to the network. Accordingly, QR believes that there needs to be greater flexibility in charging arrangements for major customers, who are distinguished by their sensitivity to TUoS charges.

QR believes that regulators should avoid giving distributional objectives weight in their decision making – especially if doing so is at the cost of economic efficiency. The long term interests of society are advanced by establishing a stable regulatory environment that operates to advance the general economic welfare of the nation – pursuing sectoral interests beyond this is likely to be counter to efficiency objectives and hence the welfare of the

community as a whole. QR believes that minimising the regulatory risk for TNSPs is critical to producing such an outcome.

Chapter 4 – Current Transmission Pricing Regime

QR believes that the critical issue associated with any pricing regime is to ensure it is efficient and capable of delivering the long term dynamic efficiency gains that are critical to maintaining Australia's economic performance. After all, the very rationale for the creation of the NEM (and the whole microeconomic reform process) has been to improve Australia's living standards – a key element of which involves enhancing our capacity to compete internationally - whether for exports or for new investments.

As such, to the extent possible, prices should reflect underlying cost drivers with a clear identification of common service costs and the recovery of such fixed costs in the least distortionary manner possible. This in turn suggests that the bulk of fixed and common costs should be recovered from customers who are least sensitive to these charges.

QR has limited experience with the CRNP and modified CRNP approaches. However, QR notes that rail access pricing typically operates between a floor and a ceiling. QR submits that this concept is worthy of consideration in the context of transmission charging. In other words, for major customers there is merit in informing pricing decisions by considering the incremental costs of supply.

It is in this context that QR believes that the continued inclusion of TUoS discounting within the Rules is critical to delivering efficient outcomes. For the reasons outlined above, these discounts can be critical to enabling major energy users to access competitive energy costs in a global market for such major investments and are therefore critical to support Australia's competitive position.

However, as noted above, QR does not consider that the current discounting arrangements will deliver the optimum outcome as they are likely to result in some projects not progressing due to transmission charges resulting in total energy costs being too high. Discounting should be encouraged where it is efficient to do so – namely, where it is necessary to attract additional load to or retain existing load for the network (consistent with, at a minimum, covering at least the incremental costs associated with servicing the load).

Simply including the possibility of providing TUoS discounts to an incremental cost level within the Rules is unlikely to mean that such a level of discount is able to be accessed by customers. Firstly, TNSPs will need to be confident that where they offer a discount that at least covers the long run incremental cost expected at the time the discount was negotiated they will not be subsequently financially disadvantaged through a regulatory review. In addition, for the reasons outlined above, the continued reliance on a revenue cap form of price control may not provide sufficient incentives to ensure that efficient discounts will always be offered, and as such, it is considered that customers should be able to access dispute resolution mechanism where negotiations with the TNSP fail to deliver an acceptable outcome.

Finally, it is critical that the discount is provided over a sufficiently long period to underpin the investment in question – it is understood that the period of certainty for discounts under the current regime could be limited to the current regulatory period, which is clearly an insufficient period to underpin energy price sensitive investments.

Chapter 5 – Efficiency and Transmission Pricing – Key Concepts

As discussed above, QR believes that the overarching aim of transmission pricing should be to deliver economic efficiency (and that the interpretation of the long term interests of consumers should be read in this light). QR notes that excessive focus on sectoral interests can distort decision making in a way that is inimical to the promotion of the economic welfare of Australians generally.

QR notes that constraints can emerge in the short term as well as in the long term. QR believes that the nature of the price signals that are sent need to relate to the impact of the constraint that is being experienced. Accordingly, QR believes that long run incremental cost assessments should be informed by the forward looking long run costs of network expansion. Short term constraints (manifesting in congestion and increased marginal losses) are best addressed through shorter term price signalling.

Chapter 6 – Relevant NEM Context

QR notes that it is an accepted practice of rail pricing in Australia that infrastructure charges should be between a floor (defined by incremental cost) and a ceiling (based on stand alone cost). These concepts could also usefully inform transmission pricing – noting that the transactions costs associated with the market can properly require a relatively prescriptive approach applying to transmission charges for the majority of customers.

Chapter 7 – Allocation of Regulated Revenue Across Transmission Users

QR supports TNSPs being given high levels of discretion to negotiate discounted charges provided it can demonstrate that the discount was considered to be reasonable in order to attract the load and that incremental costs were recovered. This discretion should be part of the normal commercial negotiations undertaken between the TNSP and customer with access to dispute resolution in circumstances where negotiations do not deliver an acceptable outcome.

Clearly, it is essential that any such discount does not financially disadvantage the TNSP. The requirement that transmission charges at least recover incremental costs should ensure that this is the case for all new connections. For those limited instances where a case can be made for a discount to apply to an existing load, then any shortfall in revenues should be able to be recovered from other loads.

Chapter 8 – Structure of Prices

QR believes that the bulk of fixed and common costs should be recovered from customers who are least sensitive to these charges. Where transmission charges are discounted, it is appropriate that the structure of charges reflects the discount that is provided (so that if

incremental costs are levied, then the structure of the charging should signal the impact of the additional consumption – which is most likely to be capacity based).

Chapter 9 – Pricing of Non-prescribed Services

QR considers that pricing of non-prescribed services should be largely on the basis of commercial negotiation between the parties with access to suitable dispute resolution where appropriate.

Chapter 10 – Inter-regional Issues

QR generally supports the move to a more consistent basis for establishing transmission prices across the NEM including with respect to inter-regional transfers. Clearly, at a minimum this should be based on ensuring that importing regions at least cover the incremental costs they impose on the network.

Yours sincerely

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9 January 2006