

20 October 2006

Dr John Tamblyn
Chairman
Australian Energy Market Commission
By email to submissions@aemc.gov.au

Dear Dr Tamblyn

Thank you for the opportunity to make a further contribution to the Australian Energy Market Commission's (AEMC) consideration of the economic regulation of transmission services.

The Consumer Utilities Advocacy Centre Ltd (CUAC) is an independent advocacy organisation, established to represent the interests of Victorian consumers, particularly low-income, disadvantaged, rural and regional and Indigenous consumers, in policy and regulatory decisions on electricity, gas and water. This submission has been made with the interests of those consumers in mind.

This submission focuses on the issues raised by the Commission on its website, and particularly whether the Rules should provide that:

- a transmission network service provider's (TNSP) proposal must be accepted if the Australian Energy Regulator (AER) is satisfied that the proposal for forecast expenditure satisfies the criteria in the Rules; or
- the AER should have a residual discretion to substitute its own reasonable estimate of forecast expenditure in those circumstances.

CUAC continues to have concerns that the Commission's decision to require the TNSP and AER to determine a 'reasonable estimate' of future expenditure intrinsically weights the decision in favour of the business, and against consumers' interests.

CUAC does not agree with the position outlined by the Commission, particularly that the draft Rules provide "the regulator with sufficient power and safeguards to be able to achieve regulatory outcomes that are not overly distorted by strategic behaviour on the part of TNSPs" (p 52).

The concept of ‘reasonable estimate’ remains too broad to provide sufficient guidance and discretion to the regulator in making a price determination in accordance with the NEM objective (i.e. in the long term interests of consumers).

CUAC’s view is supported in the advice provided to the Commonwealth by the Australian Government Solicitor: “the use of the ‘reasonable estimate’ test, uncertainty in forecasting, the existing case law in *Gasnet* and *Telstra* and the role of the pricing principles in resolving conflict, will result in the AER being required to accept a range of forecasts higher than those it would determine as the most appropriate or best estimate.” (p 19)

As noted in our previous submission, CUAC prefers the formulation put forward by the Expert Panel: “best estimate arrived at on a reasonable basis’. That formulation rightly places the onus for proof upon the TNSP, and requires it to make a robust case for its forecasts. We are not convinced that the ‘reasonable estimate’ test requires an equal rigour from the TNSPs.

The ‘reasonable estimate’ test also clearly carries with it implicit incentives for businesses to put forward costs at the higher end of a ‘reasonable’ range – that means putting up prices for consumers, with no added value or return to them. The inherent inequity of such a decision making process was identified by the Australian Government Solicitor:

“[68.] The AER’s discretion both to accept a total as a best estimate, or impose a best estimate, will result in more symmetrical review rights for users and service providers as opposed to a test based on a reasonable estimate.” (p 22).

CUAC agrees with the Commission that incentives for strategic behaviour by regulated entities are a reality in a regulatory process. But it must be remembered that the cost of that behaviour is ultimately borne by consumers, who have no ability to choose alternate suppliers and very limited capacity to question those costs. Consumers therefore rely heavily on the regulator to ensure that prices are fair. As such, CUAC strongly believes that regulators must have sufficient authority to identify and minimize gaming by regulated entities. We do not believe that the draft Rules convey that authority to the AER.

As we noted in our previous submission, Victorian consumers expect a range of outcomes from the economic regulation of TNSPs: continued access to reliable and affordable electricity; efficient market structures; transparent and accountable decision-making; and, as is implicit within the NEM objective, that the public interest remains the prime imperative for decision-making.

It is therefore crucial for the interests of consumers that there exists a robust process for making price determinations, which does not weight the interests of regulated businesses over those of their customers. CUAC strongly recommends that the Commission give further consideration to its decision, to ensure that the draft Rules adequately achieve those outcomes.

April 7, 2006

In summary, therefore, CUAC recommends the following

- the AER should be able to reject costs that are not a 'best estimate arrived at on a reasonable basis'; and
- in that event, the AER should be able to substitute its own best estimate.

Please contact me on (03) 9639 7600 should you have any questions about this submission.

Yours sincerely

Kerry Connors
Executive Officer