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8 May 2015

John Pierce
Chairman
Australian Energy Markets Commission
PO BOX A2449
SYDNEY SOUTH, NSW 1235

Dear Mr Pierce

Re: Submission on tariff alignment rule change

The AER welcomes the opportunity to comment on the AEMC's consultation paper on changes proposed to the National Electricity Rules in relation to aligning network and retail tariff structures for small customers.

The AEMC's consultation paper demonstrates a level of apprehension as to the merit of this rule change proposal. We share the same overall concerns with supporting a rule change premised on making departures from nationally consistent pricing rules, and designed to try and mitigate the impact of these departures. We agree with the AEMC that:

- The circumstances identified by the rule proponents as necessitating tariff structure impositions might more efficiently be dealt with via the new national distribution pricing arrangements.
- Imposing tariff structures on businesses would be at odds with the intent of these new arrangements and could result in greater unpredictability in electricity pricing.

Consistency with national pricing arrangements

The new distribution pricing arrangements introduced in November 2014, provide a nationally consistent framework to guide moves toward greater cost reflectivity in network prices and ultimately the price signals passed onto consumers by retailers. The tariff alignment rule change appears to be premised on a need for jurisdictions to impose particular tariff structures on retailers and therefore distributors, to manage the impact on customers of transitions toward cost reflective prices. This relates particularly to small customers who have access to interval metering. However, in our view the new distribution pricing rules appear to provide a robust and preferable framework for managing these issues:

- Distributors will be required to directly consider the impacts on customers of their tariffs, including the need to manage the transition process. This includes the ability to transition customers over a number of years, as determined in consultation with their stakeholders (retailers and consumers). We will also be able to provide oversight of how these issues were considered with stakeholders, when we review distributor tariff proposals.

- In designing their tariff structures, distributors will need to consider the ability of particular customers to respond to those structures.

We acknowledge that these features of the national distribution pricing arrangements were not present in the framework that existed prior to the AEMC's final determination in November 2014. We also note that the final determination was completed after the tariff alignment rule change was proposed. In this regard, there should be consideration on the effectiveness of the new pricing requirements in addressing the concerns that this tariff alignment proposal also purports to address.

Further, imposing particular tariff structures as intended by the rule proponents, appears at odds with some of the central features of the new distribution pricing arrangements. These arrangements intend instead to provide distributors with ownership of their tariff structures, and for these to evolve and be customised to particular demand conditions within their networks.

Implications for national distribution pricing rules

It is difficult to anticipate the exact nature of the particular tariff structures that jurisdictions might seek to impose. This makes it difficult to definitively foresee the effects on our application of the distribution pricing arrangements. There is the possibility, as identified in the AEMC's consultation paper that tariff structures imposed by jurisdictions would not be cost reflective and be inconsistent with obligations on distributors in applying the new pricing objective and efficiency based pricing principles.

The imposition of any new regulatory obligations with respect to tariff offerings should ideally be subject to consideration under the national rules and law, of the resulting costs and benefits. Regardless of the type of tariff structure that is imposed, there is a risk that this could confuse price signals by affecting the overall cost reflectivity of all network tariffs, increasing unpredictability in pricing and imposing administrative costs on distributors and retailers, as follows:

- Depending on the type of tariff structure that is imposed, distributors might need to reallocate their intended cost recovery from customers that are to take up this tariff. For example, lowering cost recovery from these customers would require recovering more from customers on other tariffs. This would affect the degree to which prices inform on the impact of electricity usage decisions of all customers, not just those receiving the imposed tariff structure. The new distribution pricing rules allow departures from efficiency to the minimum extent necessary to comply with jurisdictional obligations. However, the reallocation of costs that could be required to accommodate these obligations might represent significant departures from cost reflectivity.

- Distributors might also have difficulty in predicting the exact number of customers who will take up the imposed tariff structure. This means that cost recovery between tariffs could end up needing to be higher or lower than was anticipated for that particular year. In such situations, customers could face more volatile price level movements as distributors seek to account for over and under recovery of costs.

- If a distributor was required to offer a particular tariff structure and therefore reallocate its intended cost recovery in a significant way, this would presumably trigger a change to their Tariff Structure Statements (TSS) - which under the new arrangements they will be required to prepare for a five year period as a starting point. More frequent TSS changes will also add further pricing unpredictability for the market – one of the issues that the new pricing arrangements aimed to address. Further, at a more practical level, the administrative costs on both distributors and us in assessing more frequent TSS amendments would also increase.

Other issues

The AEMC's consultation paper also sought comment on the appropriate timing for introducing this rule change and the appropriate allocation of risk. The latter issue relates to the situation where jurisdictions have decided to impose tariff structures on retailers. More specifically, whether it is appropriate for any risk to be transferred to distributors by requiring them to offer aligned tariffs as proposed, or to be transferred to retailers - as the AEMC's consultation paper suggests could result without the rule change. It is difficult to comment on these two issues as we have reservations about imposing tariff structure offerings on businesses in the first place. Further, the issue of how to manage risk and the nature of that risk could depend on the particular tariff structure that was being considered, and should appropriately be assessed at such a time. At this stage the following is unclear and could be explored:

- If and how risks for retailers vary if the imposed tariff structures were flat consumption based or time varying, and how these would differ to those that distributors might design without this rule change.

- How retailers might manage misaligned tariffs even without any tariff structures being imposed on them by jurisdictions.

We would be pleased to provide any further assistance to the Commission in its consideration of this rule change. If you would like to discuss any aspect of our submission please contact Bruno Coelho on 08 8213 3435.

Yours sincerely

Bruno Coelho (on behalf of Chris Pattas, General Manager)
Assistant Director
Networks

Sent by email on: 08.05.2015