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5 September 2007

Mr Mike Buckley
General Manager
Network Regulation North
Australian Energy Regulator
PO Box 1199
Dickson ACT 2602
By email: AERinquiry.PMG@aer.gov.au

Dear Mr. Buckley,

Transmission Pricing Methodology Guidelines

EnergyAustralia welcomes this opportunity to provide the AER with feedback on the Draft Transmission Pricing Methodology Guidelines.

EnergyAustralia is broadly supportive of these guidelines. In particular:

- EnergyAustralia welcomes the choice of two relatively simple pricing structures that are not administratively burdensome. It is also recognised that the guidelines allow for a case to be made for alternate structures to be used, and EnergyAustralia intends to work with TransGrid to maintain the current monthly demand charge that is readily translated to demand charges in distribution prices.
- EnergyAustralia is also pleased to see provision within the guidelines to accommodate confidential or commercially sensitive information. Aspects relating to individual prices and prudent discounts are commercially sensitive in nature and EnergyAustralia anticipates invoking these provisions as a result.

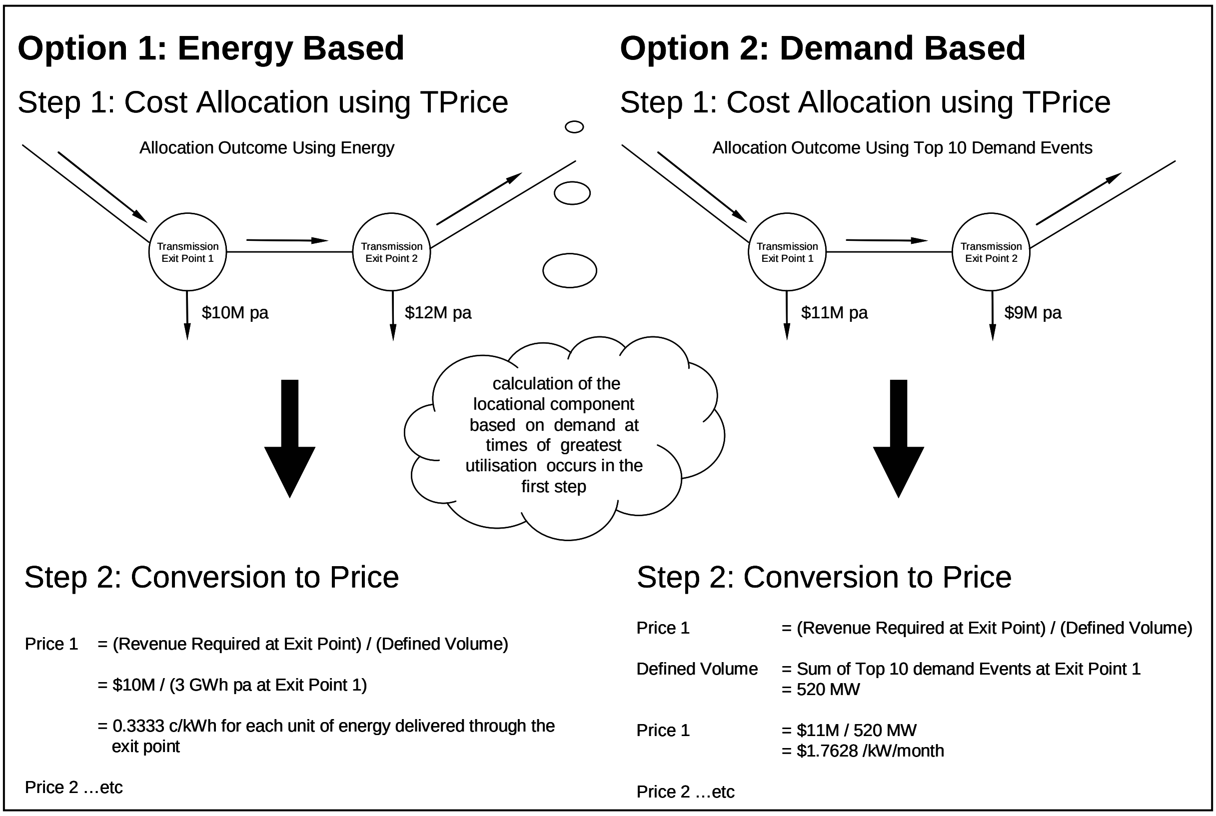
Price setting

The guidelines would benefit from a clearer distinction in the process of price setting between: the first step of cost allocation; and the second step of constructing prices.

For example, the first step in deriving prices for a location is the cost allocation and this might result in a transmission node receiving $10M in costs. But then there is a second step in constructing prices, by taking the cost allocation result of $10M and converting it in to a $/MW/month price, or some other form of price.

The diagram at top of the next page demonstrates the two step process in price setting:

Diagram 1: Options to Highlight the 2 Step Process in Price Setting



Step 1: The diagram demonstrates that cost allocation must be carried out as the first step. This cost allocation for NSW currently uses the standard TPrice allocation approach but the utilisation modified approach to allocation is used in some other jurisdictions. Two examples are shown, which highlight that the cost allocation could be based on a number of approaches.

Step 2: This is then to convert the cost allocation result to a price structure to be applied to customers. This is in fact the most significant aspect which will influence customer response. Again, two examples are given to demonstrate that this could be done a number of ways, and does not necessarily need alignment with previous cost allocation step. Indeed the cost allocation outcomes from Option 1 could then be fed in to the Conversion to Price method in Option 2, or vice versa.

As noted in the diagram, calculation of the locational component based on demand should take place in Step 1 under Option 2. But the guidelines do not prescribe this, but rather require that the price be structured on demand at Step 2. This appears to leave open the possibility of using Option 1 for cost allocation and Option 2 for conversion to price. If the policy intent is to signal peak congestion, then the drafting should reflect that Step 1 under Option 2 is what is required.

Therefore, greater clarity around sections 2.2(a), (b) and (c) of the guidelines is desirable, to specify for TNSPs those parts of the guidelines that relate to cost allocation and those which refer to price construction.

End use customer prices

While the Guidelines can only reflect the requirements in the Rules, we reiterate from our previous submission that transmission charges are seen directly by only a very few large customers and by DNSPs. To be efficient, transmission pricing structures must be capable of ready translation into prices which can influence customers' consumption patterns. As detailed in our earlier submission, large customers where such locational price signals can be passed directly to, only make about 18% of energy through the transmission network. Most transmission demand is driven by end use distribution customers with peaky summer loads. Indeed, large customers with locational signals applied to them are generally highly energy intensive, with flat load profiles, and price signalling to them may be of little benefit. That is, the real efficiency in price signalling is in being able to signal transmission costs to domestic and small businesses connected on the 11kV and 415V distribution networks. As proposed, the draft guidelines leave DNSPs in the position of simply absorbing the price signals, since there is no way of translating the permitted structures to end use customers. No efficiency will be gained in moving away from current practice to those proposed in the guidelines.

Other matters

In relation to confidentiality, the drafting of the guidelines may not comply with the requirements of the Rules. Rule 6A.25.2(e) requires the guidelines to specify those parts (if any) of a proposed pricing methodology or the information to accompany it, that will not be publicly disclosed without the consent of the TNSP. Section 2.5 of the Guidelines is headed "Disclosure of Information" but it does not actually specify when the AER will not disclose information.

There are a few (relatively minor) matters which the guidelines are purporting to require in TNSP methodologies (mainly by way of information) which are not supported by Rule 6A.25. These are in section 2.1 (h) relating to prudent discounts, (i) relating to billing arrangements and (p) and (q) relating to monitoring and compliance with pricing methodology.

In relation to prudent discounts, these are subject to a specific AER approval process under Rule 6A.26.1, but it is not clear that this is relevant to the pricing methodology. If something is to be included it should at least refer to prudent discounts which have or which are proposed to be submitted to the AER for approval.

EnergyAustralia's view is that billing arrangements are not relevant to the pricing methodology. There may be an intention to make the methodology a general pricing information document, but that is not its purpose under the Rules.

Finally, the monitoring and compliance information required under (p) and (q) these should be specified in the information guidelines under Rules 6A.17.1 and 2.

If you have any questions regarding this submission, please feel free to contact me on 02 9269 4171 or Mr. Chris Amos, Manager – Network Pricing on 02 9269 2136.

Yours sincerely

Harry Colebourn
Executive Manager – Network Regulation & Pricing