FINAL DECISION
Ergon Energy and Energex

Distribution Determination 2020 to 2025

Attachment 18
Tariff structure statement

June 2020

AUSTRALIAN ENERGY REGULATOR

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AER reference: 62728 (Ergon Energy); and 62727 (Energex)

Note

This attachment forms part of the AER's final decisions on the distribution determinations that will apply to Ergon Energy and Energex for the 2020–25 regulatory control period.

Ergon Energy and Energex have proposed a common tariff strategy. Accordingly, our assessment is also largely common across both proposals. Considerations which are specific to one distributor has been identified. This attachment should be read with all other parts of the final decision for Ergon Energy and Energex (as the case may be).

The final decision for each distributor includes the following attachments:

Overview

Attachment 1 – Annual revenue requirement

Attachment 2 – Regulatory asset base

Attachment 3 – Rate of return

Attachment 4 – Regulatory depreciation

Attachment 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 7 – Corporate income tax

Attachment 8 – Efficiency benefit sharing scheme

Attachment 9 – Capital expenditure sharing scheme

Attachment 10 – Service target performance incentive scheme

Attachment 12 – Classification of services

Attachment 13 – Control mechanisms

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Attachment 15 – Alternative control services

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Attachment 18 – Tariff structure statement

Attachment A – Negotiating framework

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18 Tariff structure statement

This attachment sets out our final decision on Ergon Energy's and Energex's tariff structure statement (TSS) to apply to the 2020–25 regulatory control period.

A tariff structure statement applies to a distributor's tariffs for the duration of the regulatory control period. It should describe a distributor's tariff classes and structures, the distributor's policies and procedures for assigning customers to tariffs, the charging parameters for each tariff, and a description of the approach the distributor will take to setting tariff levels in annual pricing proposals. It is accompanied by an indicative pricing schedule.[1] A tariff structure statement provides consumers and retailers with certainty and transparency in relation to what network tariff structures will be charged to retailers for different types of customers over the five year period that it applies.

Ergon Energy and Energex are both part of the Energy Queensland group and have based their separate revised TSS proposals on a largely common tariff strategy across the two networks. As a result, our assessment is also largely common across both proposals. We have published this final decision attachment that covers our assessment of both Ergon Energy's and Energex's revised TSS proposals.[2] Where relevant, this attachment distinguishes elements that specifically relate to Ergon Energy, such as the tariff arrangements designed to mitigate the impact of changes in regulated retail tariff arrangements in regional Queensland.

It is important to note that distributors directly charge retailers for the network services provided to end-customers and how these network tariffs are reflected in retail tariffs depends on a mix of regulatory and market factors at the retail level. There are differences in the retail arrangements that apply in Ergon Energy's and Energex's distribution areas.

In Energex's distribution area, the structure of retail prices should be determined in the market by retailers responding to consumer preferences and competitive pressures. The purpose of network tariff reform is that distributors provide retailers with better price signals over the costs associated with the provision of electricity network services. This will ensure that retailers make informed decisions about how best to manage the financial risks under more cost reflective network pricing. The competitive retail market helps promote an outcome where retailers make these decisions in a manner that takes into account the preferences of their end-customers. In some instances, retailers could rely on non-price measures, such as well-targeted demand management initiatives, to manage these commercial risks. In other situations retailers may be encouraged to pass through cost reflective network tariff structures to end-customers if they believe that these customers are well placed to respond to these

1 NER, cl.6.18.1A(a).

2 For simplicity, for elements where the Queensland distributors' revised TSS proposals are the same we provide document references to the Ergon Energy version of the revised TSS proposal.

price signals and potentially be rewarded for doing so. At present, it is more common for retailers to pass through the cost reflective network tariff structures to large business customers, than for residential or small business customers.

In Ergon Energy's distribution network area, the majority of consumers are on regulated retail offers, though they can also choose a market offer. The retail tariff structure for those regulated retail offers is determined by the Queensland Competition Authority, and may not necessarily reflect the same structure as the underlying network tariff structure. The uniform tariff policy in Queensland also means that customers in Ergon Energy's distribution area face the same level of network tariffs as customers in Energex's area.

18.1 Final decision

This attachment sets out our final decision on the Queensland distributors' tariff structure statement to apply for the 2020–25 regulatory control period.

Our final decision supports the majority of Energex's revised TSS proposal. However, we have concerns with some aspects of Energex's revised proposal.[3] In this final decision, we have therefore set out the minimum changes that we consider necessary for us to approve Energex's TSS.[4] Similarly, our final decision supports the majority of Ergon Energy's revised TSS proposal. However, we have concerns with some aspects of Ergon Energy's revised proposal.[5] In this final decision, we have therefore set out the minimum changes that we consider necessary for us to approve Ergon Energy's TSS.[6] There are also some minor wording changes we have made to the revised TSS proposals of the Queensland distributors to improve the clarity and completeness of the TSS's.

We publish the final version of the TSS for Energex and Ergon Energy alongside this decision. For transparency, we publish both a clean version and a version which is marked-up from the revised TSS proposal submitted by each of the Queensland distributors.

Our final distribution determination for the Queensland distributors was delayed from 30 April 2020 to 5 June 2020 to allow us to include a more accurate forecast of inflation. However, to aid transparency and to assist stakeholders to prepare for 1 July network price changes, we committed to publishing a number of documents in advance of this decision. This included an indicative final version of the TSS for each Queensland distributor which were published in May 2020. Our final TSS for each Queensland distributor is consistent with the indicative final TSS we previously published except for minor corrections and to address typographical errors and formatting issues.

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3 NER, cl.6.18.5.
4 NER, cl.6.18.5(d).
5 NER, cl.6.18.5.
6 NER, cl.6.18.5(d).

The following table summarises our final decision on elements of the Queensland distributors' revised TSS proposals. This comprises:

- Matters where our draft decision required changes to the distributors' initial TSS proposal which the distributors' adopted in their revised TSS proposal. In these cases, we have generally accepted the revised proposals subject to our consideration of any stakeholder submissions on these matters.
- Matters where our draft decision required changes to the distributors' initial TSS proposals which the distributors' responded to in their revised TSS proposal, and where the distributors' response has required further assessment by us.
- Matters which arose subsequent to our draft decision (e.g. our response to COVID-19).

Table 1: Overview of the key issues raised in the Queensland distributors' revised TSS proposals and our final decision

Issue	Our draft Decision	Revised TSS proposals	Our final Decision
Rationale for network tariff reform	Sought greater clarity on rationale for tariff reform	Added additional text to TSS	We agree with the distributors that tariff reform is important but we have an alternative view on why it is important. We explain our view in this attachment. To understand the reasons for our decision refer to section 18.4.1 of this document
Design of default cost reflective network tariff for small users	Not approved distributors' proposed consumption tariffs as default tariffs Default tariff must have cost reflective structure. Required removal of daytime demand charge.	Agreed with AER Adopted transitional demand tariff as default tariff	Approved as revised proposals address the concerns in our draft decision. No amendments required.
Implementation timing of reforms to default cost reflective network tariffs for small users	Not approved distributors' proposed opt-in approach to implementation A 12 month grace period should apply to existing customers with smart meter on a legacy consumption tariff.	Partially agreed with AER. 12 month grace period applied to existing customers with smart metering New and existing customers that received smart meter from 1 July 2020 to be immediately reassigned to transitional demand tariff	Approved 12 month grace period for existing customers with smart meter installed prior to 1 July 2020. Approved immediate assignment to transitional demand tariff of new and existing customers that upgrade to smart metering from 1 July 2020, amended to apply to customer initiated upgrades. Amended TSS to also apply 12 month grace period to customers that receive

Issue	Our draft Decision	Revised TSS proposals	Our final Decision
		Legacy consumption tariffs closed from 1 July 2020	a smart meter due to replacement reasons.[7] To understand the reason for our decision refer to section 18.4.3 of this decision. Amended TSS to allow customers to temporarily opt-out to legacy consumption tariffs in 2020–21 to mitigate impact of covid-19 pandemic.[8]To understand the reasons for our decision refer to section 18.4.4 of this document.
The need to provide retailers with a choice of cost reflective tariff structures	Required that time of use tariffs be introduced on an opt-in basis from 1 July 2020.	Agreed with AER Proposed new time of use energy tariffs on an opt-in basis	Approved as revised proposals address the concerns in our draft decision. No amendments required. To understand the reasons for our decision refer to section 18.4.5 of this document.
Methodology for LRMC estimation	Raised concern over some aspects of the proposed approach to estimating LRMC. Encouraged Queensland distributors to make future improvements in this approach.	Agreed with the AER The Queensland distributors commit to revisiting this approach in next round of TSS covering 2025–30 regulatory control period.	Approved as revised proposals address the concerns in our draft decision. No amendments required. To understand the reasons for our decision refer to section 18.4.6 of this document.
The introduction of capacity tariffs	Not approved proposal to introduce new capacity tariffs on an opt-in basis. Encouraged capacity tariff trial to be undertaken in 2020–25 regulatory control period.	Agreed with AER Withdrew capacity tariff proposal Committed to undertaking capacity tariff trial.	Approved as revised proposals address the concerns in our draft decision. No amendments required. To understand the reasons for our decision refer to section 18.4.7 of this document.
Addressing the impact of existing customers being reclassified from small to large.	Concern that IBT proposal could exacerbate bill shocks for customers reassigned to demand tariff due to exceeding 100 MWh pa Encourage the Queensland	Agreed with AER Proposed Wide Inclining Fixed Tariff for basic metered customers consuming greater than 20 MWh pa.	Approved introduction of WIFT from 1 July 2020. Amended TSS to require that the Queensland distributors introduce specific new tariff for basic metered customers assessed as consuming more than 100 MWh pa from 1 July 2021. To understand the reasons for our decision refer to section 18.4.8 of this

[7] The requirement applies to the Queensland distributors on a reasonable endeavours basis.

[8] The Queensland distributors are required to reassign customers with smart metering on legacy consumption tariff to the transitional demand tariff on 1 July 2021, except where customer is subject to grace period provision.

Issue	Our draft Decision	Revised TSS proposals	Our final Decision
	distributors to address concerns in revised TSS.		document.
The introduction of new controlled load tariffs	Support in principle but not convinced that these tariffs comply with the NER. Sought greater clarity on terms and conditions of these tariffs	Agreed with AER Provided additional text on rationale for new controlled load tariff	Approved with additional obligations imposed[9] To understand the reasons for our decision refer to section 18.4.9 of this document.
To allow hardship customers to opt-in to legacy consumption tariff	Not approved due to lack of evidence that this proposal is required to mitigate the impact on cost reflective pricing on hardship customers.	Agreed with AER. Withdrew this proposal.	No further action required.[10]
Grandfathering or retirement of existing legacy seasonal cost reflective tariffs	Not convinced that this proposal complies with the NER given that these tariffs have a seasonal basis which is cost reflective.	Disagreed with AER No change proposed to this element of tariff strategy	*Ergon Energy only* Amended the TSS to require that Ergon Energy offer the CAC seasonal demand tariffs on an opt-in basis from 1 July 2020. To understand the reasons for our decision refer to section 18.4.9 of this document.
The expansion of the eligibility criteria for the ICC tariff class	Agree in principle. Sought greater clarity on criteria. Raised concern over the lack of clarity in relation to the price setting approach for these tariffs.	Agreed with AER Included additional text in TSS.	Amended the TSS to remove the equity related criteria, achieve greater consistency between Queensland distributors and to improve the clarity of the description.[11] To understand the reasons for our decision refer to section 18.4.10 of this document.
Peak charging windows	Concern that broad peak charging window of cost reflective tariffs does not comply with NER.	Agreed with the AER Proposed narrower peak window	Approved as revised proposals address the concerns in our draft decision. No amendments required.
Customer impact	Sought more detailed information	Agreed with the AER	No further action required.

9 Queensland distributors are required to set out the terms and conditions of these tariffs in their 2020–21 annual pricing proposals.

10 The AER requires that the legacy consumption tariff be temporary available to all customers on an opt-in basis in 2020–21 for the purpose of mitigating the impact of the covid-19 pandemic.

11 Queensland distributors are required to set out their approach to setting ICC tariffs in their 2021–22 annual pricing proposals.

Issue	Our draft Decision	Revised TSS proposals	Our final Decision
analysis	of the impact of proposed tariffs.	Provided additional customer impact analysis in TSS.	
Managing the customer impact of expiration of transitional and obsolete retail tariffs in regional Queensland	Recognised that expiration of these regulated retail tariff arrangements is likely to create unacceptable bill shocks for some large customers.	Agreed with AER Proposed non-standard transitional ICC tariffs to manage the risk of large customer disconnecting from network or bypassing distribution network.	Amended TSS to change the basis of transitional non-standard ICC tariff to focus on mitigating customer impact by transitional the peak charge to LRMC over reasonable time frame and in recognition of localised economic conditions. To understand the reasons for our decision refer to section 18.4.11 of this document.
Excess demand charges for large business customers	Concern over the lack of clarity over the excess kVA charge proposal	Agreed with AER. Provided additional clarity on this aspect of the TSS.	Approved removal of excess kVA charge. Approved excess demand charge proposal but: • Queensland distributors are to address our concern over efficiency properties of this charging parameter in the next round of TSS proposals. • The DUoS price level of this charging parameter is not to exceed 30% of the applicable LRMC estimate, except where required to mitigate customer impact. To understand the reasons for our decision refer to section 18.4.12 of this document.
Addressing potential non-compliance in previous regulatory control period	Issue not raised in initial proposal	The Queensland distribution raise the existence of network tariffs that do not comply with current TSS and seek to work with the AER towards addressing this issue.	We require the Queensland distributors to complete a review of their network pricing and billing arrangements by 31 December 2020 on a reasonable endeavours basis. To understand the reasons for our decision refer to section 18.4.13 of this document.

Source: AER analysis

Obligation to finalise certain tariff matters at the annual pricing proposal stage

There are a couple of matters where our final decision establishes an overarching position and requires further detail to be proposed by the Queensland distributors' at the annual pricing proposal stage for further assessment by the AER. These are matters that arose after our draft decision, or as a result of the Queensland distributors' response to our draft decision, and where we have formed an overarching position but more work will be required to implement these positions.

An annual pricing proposal must demonstrate compliance with the distributor's TSS.[12] Accordingly, the Queensland distributors will be required to address the following matters in their future annual pricing proposals in order for us to approve the annual pricing proposals as compliant with the distributors' TSS.

The following table provides a summary of these obligations.

Table 2: Obligations on the Queensland distributors on tariff matters to address in annual pricing proposals

Distributor	Tariff matter	Obligations on annual pricing proposals
Energex and Ergon Energy	The introduction of new controlled load tariffs	Our final decision approves the introduction of new controlled load tariffs. Our decision requires the Queensland distributors to set out the terms and conditions of these tariffs in their 2020–21 annual pricing proposals.
Energex and Ergon Energy	Individual Customer Connection (ICC) tariffs	Our final decision requires the Queensland distributors' approach to setting ICC tariffs to be based on transitioning the LRMC component of tariffs towards cost reflectivity over time, and requires the option of allowing users to choose to pass through of the location-specific component of Powerlink's transmission charges. However, our decision does not fully specify the approach to setting these tariffs, Instead, our final decision requires the distributors to include in their pricing proposals for the 2021–22 regulatory year (and subsequent regulatory years) a more detailed description of the approach to setting the ICC tariffs.
Energex and Ergon Energy	SAC large tariffs	Our final decision requires the distributors to introduce new tariffs to apply to residential and business customers with basic metering that are assessed as consuming above 100 MWh pa from 1 July 2021. Our decision requires these tariffs to be based on the customers' actual usage and be of flat or block design. However, our final decision does not prescriptively specify the structure for these tariffs. Instead, our decision requires the distributors to include the detailed tariff structure for these tariffs within their 2021–22 annual pricing proposals (and annual pricing proposals for subsequent years).
Energex and Ergon Energy	Legacy tariff arrangements	In their revised proposals, the distributors identified that there had been some areas where they had not been fully compliant with the 2017-20 TSS. As this stage, the distributors have not proposed any actions to address this historical non-compliance. Our final decision requires the distributors to complete a review of their network pricing and billing arrangements on a reasonable endeavours basis by no later than 31 December 2020. The purpose of this review is as follows: 1. Identify legacy network tariffs and the number of customers on these tariff arrangements; 2. Assess the extent that these customers have been over or

[12] NER, cl.6.18.2(b)(7).

Distributor	Tariff matter	Obligations on annual pricing proposals
		under charged at the NUOS level in a historical context. 3. To work with relevant stakeholders to develop a plan to: • Address any historical over billing of NUOS charges to the extent that it is reasonable to do so; • Mitigate the impact of reassigning these customers to an appropriate default network tariff in the future. Our decision requires the distributors to include the outcome of this review in their 2021–22 annual pricing proposals (and subsequent annual pricing proposals, as appropriate).

Source: AER analysis

Recommendations to process certain tariff matters during the regulatory control period

While not formal requirements of this final decision, we also encourage the Queensland distributors to process the following tariff matters during the 2020–25 regulatory control period:

- Tariff education - The Queensland distributors have proposed to support the introduction of tariff reform through their Tariff Education and Dynamic Incentive (TEDI) initiative during the 2020–25 regulatory control period. We agree with QCOSS on the importance of this program and encourage the Queensland distributors to implement this program without delay.
- Capacity tariff trial - The Queensland distributors proposed a capacity tariff in their initial TSS proposals which we did not approve because we considered the design of this tariff required further work. The Queensland distributors withdrew this tariff from their revised proposals, and have instead flagged the intention to conduct capacity tariff trials during the 2020–25 regulatory control period, noting their long term vision remains centred on capacity tariffs. We encourage the distributors to proceed with these capacity tariff trials. These trials can help provide an evidence base to design appropriate capacity tariffs for inclusion in the distributors' 2025–30 TSS proposals for assessment by the AER at that time. Without these trials, the distributors may find themselves in a similar situation to this time where there was not a strong enough evidence base to support a capacity tariff proposal for small customer network tariffs.
- Estimation methodology for LRMC - While we accept on balance the Queensland distributor's LRMC estimation methodology as being fit for purpose at this stage of tariff reform, we remain concerned over some aspects of this approach. We consider the LRIC framework is appropriate in an environment of increasing demand and expenditure. We therefore encourage the Queensland distributors to explore the implications of stagnant or declining demand growth in their LRMC estimation framework, such as by including repex into the LRMC calculation in such an environment.

18.2 Ergon Energy's and Energex's revised proposals

The Queensland distributors have based their revised TSS proposals to a large extent on a common tariff strategy across Energex and Ergon Energy.

The key elements of Queensland distributor's revised tariff structure statements that are based on a common approach are summarised below:

- Adopting a demand tariff as the default network tariff for all new residential and small business customers and existing customers that upgrade to a smart meter from 1 July 2020
- Designing the default demand tariff on a transitional basis to ensure that the introduction of more cost reflective network pricing does not cause unacceptable impacts on retailers;
- Providing retailers with a choice of cost reflective network tariffs to ensure that they are well placed to satisfy the tariff preferences of their customers by introducing time of use energy tariffs and cost reflective demand tariffs on an opt-in basis on 1 July 2020;
- Adoption of a peak charging window to apply to the proposed cost reflective tariffs for residential and small business customers that better targets the evening peak period.
- Introducing new load control tariffs for business customers on an opt-in basis.
- To minimise the impact of the introduction of cost reflective pricing at the network level by delaying the reassignment of existing residential and small business customers with smart metering to the default transitional demand tariff until 1 July 2021.
- To mitigate the impact of covid-19 pandemic by temporarily allowing retailers to reassign residential and small business customers on cost reflective tariffs to a consumption tariff until 30 June 2021.
- Expanding the eligibility criteria for the Individual Customer Calculation (ICC) tariff class to allow more large business customers to opt-in to a site-specific individually calculated tariff.

We note that there are some elements of the Ergon Energy TSS that are different to the Energex TSS. These elements are summarised below:

- Ergon Energy proposed a significant reduction in the number of tariff classes to better align with the Energex tariff class definitions;
- The introduction of opt-in time of use energy tariffs for SAC large customers impacted by the expiration of obsolete and transitional regulated retail tariffs on 1 July 2021.
- Allowing eligible large customers to opt-in to a non-standard site-specific individually calculated tariff where necessary to mitigate the impact of cost reflective pricing.

- The retention of existing legacy seasonal demand tariff for customers in the CAC tariff class on a voluntarily opt-in basis.

18.3 Assessment approach

This section outlines our approach to tariff structure statement assessments.

There are two sets of requirements for tariff structure statements. First, the NER set out a number of elements that an approved tariff structure statement must contain.[13] Second, a tariff structure statement must also comply with the distribution pricing principles.[14]

Our assessment approach for the Queensland distributors is to generally accept elements of their revised TSS proposals that are consistent with the guidance provided by the AER in our draft TSS decision.

Where a Queensland distributor has chosen to not accept our guidance or to propose a change to tariffs not covered by our draft TSS decision we have assessed these elements of the revised TSS against the distribution pricing principles in the Rules.

It should also be noted that we have also made amendments to the revised TSS proposals to the extent necessary to mitigate the potential impacts of the covid-19 pandemic on the Queensland distributors, retailers and end-customers. This has been required to satisfy the customer impact principle in the Rules.

18.3.1 What must a tariff structure statement contain?

The Rules require a tariff structure statement to include:[15]

- the tariff classes into which retail customers for direct control services will be divided;
- the policies and procedures the distributor will apply for assigning retail customers to tariffs or reassigning retail customers from one tariff to another;
- structures for each proposed tariff;
- charging parameters for each proposed tariff, and
- a description of the approach that the distributor will take in setting the price level of their tariffs in the pricing proposal for each regulatory year during the 2020–25 regulatory control period.

A distributor's tariff structure statement must be accompanied by an indicative pricing schedule with the tariff structure statement.43[16] This schedule guides stakeholder

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13 NER, cl.6.18.1A(a).
14 NER, cl.6.18.1A(b).
15 NER, cl.6.18.1A(a).
16 NER, cl.6.18.1A(e).

expectations about annual changes in the price level of network tariffs over the 2020–25 regulatory control period. As a result, we require that the annual prices in the indicative pricing schedule be based on the proposed methodologies in the tariff structure statement for signalling long run marginal costs and the efficient recovery of residual costs.

18.3.2 What must a tariff structure statement comply with?

A tariff structure statement must comply with the distribution pricing principles for direct standard control services.[17] These may be summarised as:

- for each tariff class, expected revenue to be recovered from customers must be between the stand alone cost of serving those customers and the avoidable cost of not serving those customers.[18]
- each tariff must be based on the long run marginal cost of serving those customers, with the method of calculation and its application determined with regard to the costs and benefits of that method, the costs of meeting demand from those customers at peak network utilisation times, and customer location.[19]
- expected revenue from each tariff must reflect the distributor's efficient costs, permit the distributor to recover revenue consistent with the applicable distribution determination, and minimise distortions to efficient price signals.[20]
- distributors must consider the impact on customers of tariff changes and may depart from efficient tariffs, if reasonably necessary having regard to:[21]
    - the desirability for efficient tariffs and the need for a reasonable transition period (that may extend over one or more regulatory periods).
    - the extent of customer choice of tariffs.
    - the extent to which customers can mitigate tariff impacts by their consumption.
- tariff structures must be reasonably capable of being understood by retail customers assigned to that tariff.[22]
- tariffs must otherwise comply with the Rules and all applicable regulatory requirements.[23]

The tariff structure statement must comply with the distribution pricing principles in a manner that will contribute to the achievement of the network pricing objective:[24]

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17 NER, cl.6.18.1A(b).
18 NER, cl.6.18.5(e).
19 NER, cl.6.18.5(f).
20 NER, cl.6.18.5(g).
21 NER, cl.6.18.5(h).
22 NER, cl.6.18.5(i).
23 NER, cl. 6.18.5(k).
24 NER, cl.6.18.5(j): this requirement includes jurisdictional requirements

The network pricing objective is that the tariffs that a DNSP charges in respect of its provision of direct control services should reflect the DNSP's efficient costs of providing those services to the retail customer.[25]

18.3.3 What happens after a tariff structure is approved?

Once approved, a tariff structure statement will remain in effect for the relevant regulatory control period. The distributor must comply with the approved tariff structure statement and be consistent with the indicative pricing schedule when setting prices annually for direct control services.[26]

We will separately assess the distributor's annual tariff proposals for the coming 12 months. Our assessment of annual tariff proposals will be consistent with the requirements of the relevant approved tariff structure statement.

An approved tariff structure statement may only be amended within a regulatory control period with our approval.[27] We will approve an amendment if the distributor demonstrates that an event has occurred that was beyond its control and which it could not have foreseen, and that the occurrence of the event means that the amended tariff structure statement materially better complies with the distribution pricing principles.[28]

18.4 Reasons for final decision

In this section, we outline our reasons for our final decision on the Queensland distributor's TSS to apply to the 2020–25 regulatory control period.

In our draft TSS decision, we provided the Queensland distributors with considerable guidance on what changes were required to their initial TSS proposals to achieve compliance with the pricing principles in the NER.[29] The revised TSS proposals are largely consistent with this guidance.[30] As a result our final decisions supports the majority of the Queensland distributors' revised TSS proposals. Nevertheless we have concerns with some aspects of the revised TSS.[31] To address these concerns, we have made amendments that we consider necessary for us to approve the TSS's. There are also some minor wording changes we have made to improve clarity in a few areas of the TSS.

This section sets out our reasoning on:

- Our view on why network tariff reform in Queensland is important
- Design of default cost reflective network tariff for small users

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25 NER, cl.6.18.5(d).
26 NER, cl.6.18.1B.
27 NER, cl.6.18.1B.
28 NER, cl.6.18.1B(d).
29 AER, *Draft Decision - Ergon Energy distribution determination - Attachment 18 - TSS*, October 2019, Table 18.1.
30 Ergon Energy, *Revised Tariff Structure Statement - Explanatory Notes*, December 2019, Appendix B.
31 NER, cl. 6.18.5.

- Implementation timing of reforms to default cost reflective network tariffs for small users
- The need to provide retailers with a choice of cost reflective tariff structures
- Methodology for LRMC estimation
- Capacity tariff trials
- Addressing the impact of existing customers being reclassified from small to large
- The introduction of new controlled load tariffs
- To allow some customers to opt-in to legacy consumption tariffs
- Grandfathering or retirement of existing legacy seasonal cost reflective tariffs
- The expansion of the eligibility criteria for the ICC tariff class
- Peak charging windows
- Customer impact analysis
- Managing the customer impact of expiration of transitional and obsolete retail tariffs in regional Queensland
- Excess demand charges for large business customers
- Addressing potential non-compliance in previous regulatory control period

Our reasoning for the key elements of the TSS for the Queensland distributors is discussed in more detail below.

18.4.1 Our view on why network tariff reform in Queensland is important

We and the Queensland distributors both consider network reform is important. However, we have somewhat different views on why it is important. In this section, we outline the Queensland distributors' views, stakeholders views' and our own views.

The Queensland distributors are at the forefront of the consumer driven and technology enabled transformation of the energy sector in Australia with a high number of rooftop solar PV systems installed in the National Electricity Market (NEM). This transformation is expected to continue with forecast growth in installation of solar PV systems. There is also expected to be a significant uptake over the long term of batteries and electric vehicles, albeit from a low base.

They are leading the industry in the use of automated load control in the residential and small business customer segment. We support their efforts to expand the use of controlled load products to assist consumers to improve the utilisation of their electricity distribution network.

The rapid transformation of the energy sector is changing the way that consumers are using the electricity network. The Queensland distributors believe this transformation has resulted in an exacerbation of the inherent cross subsidies under existing legacy

consumption tariffs, particularly in regard to solar PV customers[32]. As a consequence, they believe there is an urgent need to introduce demand tariffs as a stepping stone to its longer term solution of capacity tariffs.

Many of the stakeholders that participated in the engagement process for the Queensland distributors' tariff structure statements are not convinced by this rationale for tariff reform.[33][34] They do not have a clear understanding of the nature and magnitude of this cross subsidy problem, nor how the tariff reforms proposed by the Queensland distributors will address this problem.

While we and the Queensland distributors consider network tariff reform is important, our reasons for supporting network tariff reform and the majority of the Queensland distributors' revised TSS proposals reflects our own views on what we consider to be the key rationale for network tariff reform in Queensland. This is somewhat different to the Queensland distributors' reasons for their proposals which, among other matters, was framed in terms of unwinding what the Queensland distributors considers to be cross-subsidies between different consumers. Our reasons are framed more in terms of creating the right incentives on retailers and consumers for more efficient and innovative retail products and more efficient and informed end user choices in when and how they utilise the grid. In turn, we expect this to lead to more efficient utilisation of the network and network investment in the long term interests of all consumers. We explain our reasons further below.

The economic benefits of network tariff reform in Queensland are likely to be modest in the short term given the presence of excess network capacity and prospects of modest growth in peak demand. Nevertheless, we consider that the long term interests of consumers are best served by commencing the network tariff reform process in Queensland. This is because the gradual reform of network tariffs will expose retailers to increasing volume risks over time, which will encourage retailers to develop innovative ways to mitigate these risks. For customers that prefer to remain on consumption tariffs, retailers may need to rely on demand management strategies to mitigate their exposure to commercial risk created by network tariff reform. For other customers, the pass through of these risks in the form of highly cost reflective retail tariff structures represents an opportunity to be rewarded for actively managing their peak demand.

In the absence of network tariff reform, retailers are unlikely to offer consumers a choice of innovative tariffs. This is likely to mean that most consumers will continue to

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[32] Under the consumption tariff, a customer can lower their network bill by installing a solar PV system because they can reduce their energy consumption from the grid (basis of the network bill) by consuming some of the energy generated by the solar PV system. The installation of a solar PV system does not change the customer's cost to serve from a network perspective given that it does not materially reduce the customer's peak demand in the evening.

[33] ECA, *Submission on AER's issues paper on Queensland distributors' initial proposals and TSS*, June 2020.

[34] QCOSS and Etrog Consulting, *Submission on AER's draft decisions and Queensland distributors' revised proposals and TSS*, January 2020, page 15.

make investment and consumption decisions under the existing legacy consumption tariffs, even where they are willing and able to respond to more cost reflective price signals. We are concerned that this would undermine economic welfare given that retailers in this environment are less likely to actively pursue demand management strategies in the absence of being exposed to the volume risk from network tariff reform.

To be clear, we consider residential and small business consumers should continue to have the option of simple consumption based retail tariffs. The point is they should also have additional retail options which are enabled by network tariff reform. In the absence of network tariff reform, retailers will have little commercial incentive to encourage their consumers to make more efficient decisions in regard to energy investments and how they use the electricity network by passing through efficient network price signals, encouraging consumers to take-up alternative tariff options, such as controlled load tariffs, or the pursuit of well targeted localised demand management initiatives.

In light of the potential long term prospects of an upturn in electric vehicle ownership, network tariff reform can also contribute to reducing the growth in peak demand which might result, and therefore reduce the localised network congestion and need to invest in additional peak network capacity that would otherwise occur. This can be achieved through introducing more efficient peak price signals that incentivise consumers (or retailers acting on behalf of customers) to better manage the timing of their electric vehicle charging.

18.4.2 We accept the proposed transitional demand tariffs as the default tariffs for small customers from 1 July 2021

The Queensland distributors propose to adopt the transitional demand tariff as the default network tariff for all new customer connections and existing customers that upgrade to a smart meter after 30 June 2020. [35] Other types of existing customers with smart meters will be ultimately reassigned to a transitional demand tariff unless they have previously opted into an alternative cost reflective tariff, such as the (non-transitional) demand tariff or the time of use energy tariff. This element of the proposed tariff structure statement is consistent with the guidance provided in our draft TSS decision.[36]

It is important to note that the Queensland distributors responded to our concerns over their initial proposed demand tariff structure by better targeting the evening peak period.[37] We accept the Queensland distributor's argument that it is not appropriate at

[35] Note that these customers are temporarily allowed to opt-in to an applicable consumption tariff during 2020–21.

[36] AER, *Draft Decision - Ergon Energy distribution determination - Attachment 18 - TSS*, October 2019, p.28.

[37] AER, *Draft Decision - Ergon Energy distribution determination - Attachment 18 - TSS*, October 2019, p.34.

this stage of the tariff reform to adopt a seasonal basis for the default demand tariff structure.[38]

We note that some stakeholders oppose demand tariffs on the grounds that this particular tariff structure is too difficult for customers to understand and respond to. [39] These stakeholders also raise serious concerns about the economic efficiency properties of demand charges given that they are based on the individual customer's maximum demand, which may not necessarily coincide with the timing of localised critical network congestion. [40]

As stated in our draft decision, we consider that demand tariffs can be designed to be as cost reflective as time of use tariffs.[41] This is not to suggest that these tariff structures are perfectly cost reflective. Nevertheless they represent a reasonable step towards cost reflectivity for many distributors, particularly where time of use energy tariffs are also offered on an opt-in basis.

We also pointed out that in the early stages of tariff reform distributors need to be cognisant when designing their cost reflective tariffs that many of their customers have made significant investment in energy appliances in response to the incentives under existing consumption tariffs. We are satisfied that the transitional demand tariff is appropriate for the Queensland distributors given that the customer impact concerns have been addressed by transitioning the demand charge to LRMC over a reasonable timeframe. It should also be noted that the introduction of opt-in time of use energy tariffs for residential and small business customers on 1 July 2020 is likely to ensure that customers that find demand charges too complex to understand and respond to will be given a choice of cost reflective tariffs. The Queensland distributor's commitment to tariff education under their Tariff Education and Dynamic Incentive (TEDI) proposal will also support customers making informed tariff choices.[42]

18.4.3 Transitional arrangements will apply in 2020–21 to mitigate impact of Cov-19 pandemic

The Queensland distributors propose to delay the reassignment of existing residential and small business customers with a smart meter installed prior to 1 July 2020 to an applicable transitional demand tariff until 1 July 2021. As set out in our draft TSS decision we consider that the provision of a grace period under these circumstances represents a reasonable balance between the economic objective of assigning existing

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38 For an example of seasonal demand tariffs in other jurisdictions, refer to the Ausgrid 2020–21 pricing proposal. This document is available from: https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/pricing-proposals-tariffs/ausgrid-annual-pricing-2020-21

39 QCOSS and Etrog Consulting, *Submission on AER's draft decisions and Queensland distributors' revised proposals and TSS*, January 2020, Section 4.1.

40 QCOSS and Etrog Consulting, *Submission on AER's draft decisions and Queensland distributors' revised proposals and TSS,* January 2020, page 18.

41 AER, *Draft decision - Ergon Energy distribution determination - Attachment 18 - TSS*, October 2019, pp.105-106.

42 Ergon Energy, *Revised Tariff Structure Statement - Explanatory Notes*, December 2019, Appendix B.

customers to cost reflective tariffs and the need to consider the impact that this may have on customers.[43] As a result we are satisfied that this element of the revised TSS contributes to compliance with the pricing principles in the Rules.

However, we have concerns over the Queensland distributor's proposal to immediately reassign to the transitional demand tariff existing residential and small business customers that have a smart meter installed due to end of life reasons from 1 July 2020.[44] While we accept that there may be economic efficiency gains to be realised under this approach, we do not consider that this element of the revised TSS satisfies the customer impact principle in the Rules.[45] This is because customers that receive a smart meter as a consequence of the events outside their control (i.e. failure of their existing basic meter) are not likely to be actively engaged in electricity pricing issues or to fully understand their load profile or the extent that they would be willing and able to change their load profile in response to cost reflective price signals. As a consequence, customers in this situation will find it difficult to make informed retail tariff choices at short notice.

To address our concerns, we consider that it is necessary to amend the revised TSS to require that the Queensland distributors also provide a 12 month grace period to existing residential and small business customers that have their basic accumulation meter replaced due to end of life reasons after 30 June 2020.[46] We also require that the Queensland distributors give retailers the opportunity to reassign their customers to a cost reflective network tariff within this grace period. This will ensure that customers with good load profiles will not have to wait the full 12 months to realise the savings under cost reflective tariffs.

We note that some stakeholders support applying the 12 month grace period to all customers that receive a smart meter for any reason.[47] While we accept that it could be advantageous to expand the grace period to new customer connections and existing customers that upgrade to a smart meter at their request, we do not believe that it is justified to do so in order to satisfy the customer impact principle in the NER. As explained in our draft decision, we consider that these customers are better placed to understand the impact of cost reflective tariffs on their retail bills given that are more likely to be:

- Actively engaged either by investing in upgrading their connection or through considering electricity efficiency issues when preparing for a new connection.

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43 AER, *Draft Decision - Ergon Energy distribution determination* - Attachment 18 – TSS – October 2019, Table 18.1 and p.15.

44 Ergon Energy, *Revised Tariff Structure Statement*, December 2019, pp.19-20.

45 NER, cl.6.18.5(h).

46 In recognition of the practical challenges of providing a grace period of this nature we have imposed this requirement on the Queensland distributors on a reasonable endeavour basis.

47 QCOSS and Etrog Consulting, *Submission on AER's draft decisions and Queensland distributors' revised proposals and TSS*, January 2020, page 39.

- Expecting to see a change in their retail electricity bills due to the changes or upgrades to their network connection.[48]

As a result, we accept the Queensland distributor's proposal to not apply a 12 month grace period to new customers and existing customers that upgrade[49] to a smart meter from 1 July 2020 for customer initiated reasons. These customers are to be immediately assigned to the transitional demand tariff.

18.4.4 Legacy consumptions tariffs are to be offered on an opt-in basis in 2020–21

The Queensland distributors propose to close the legacy consumption tariffs for residential and small business customers from 1 July 2020.[50] We note that this element of the revised TSS is consistent with the guidance provided in our draft TSS decision and aligns with our recent TSS decisions in most other jurisdictions.[51] Nevertheless, in light of the future impact of covid-19 pandemic we consider that this proposal does not comply with the customer impact principle in the Rules.

To achieve compliance with the Rules we have amended this element of the revised TSS to keep the legacy consumption tariffs for residential and small business customers open until 1 July 2021. We consider that giving retailers the opportunity to reassign residential and small business customers on cost reflective network tariffs to the legacy consumption tariff will mitigate to some extent the impact of covid-19 pandemic, particularly for customers with high peak demand relative to their energy consumption requirement. It is important to note that this a temporary measure as we require that the Queensland distributors reassign all customers that voluntarily opt-in to a legacy consumption network tariff back to a cost reflective network tariff on 1 July 2021. We encourage retailers to work closely with their customers to ensure that they are fully informed of the retail tariff implications of this change in the underlying network tariff structure.

18.4.5 We support giving retailers a choice of cost reflective tariff structures

The Queensland distributors propose to introduce an opt-in time of use tariff for residential and small business customers from 1 July 2020.[52] This element of the TSS is consistent with the guidance provided in our draft TSS decision.[53] As a result we are

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48 AER, *Draft Decision - Ergon Energy distribution determination - Attachment 18 - TSS*, October 2019, p.28.

49 This is where the customer initiates the upgrade of their basic accumulation meter, such as for the purpose of installing a solar PV system, three phase air conditioner or electric vehicle charger (if identifiable to the distributor).

50 Ergon Energy, Revised Tariff Structure Statement, December 2019, Table 3.

51 See AER final TSS decisions for Power and Water, Ausgrid, Endeavour Energy, Evoenergy. These decisions are available from www.aer.gov.au

52 Ergon Energy, *Revised Tariff Structure Statement,* December 2019, Section 3.7.1.

53 AER, *Draft Decision - Ergon Energy distribution determination - Attachment 18 - TSS*, October 2019, pp.36-37.

satisfied that this element of the revised TSS contributes to compliance with the pricing principles in the Rules.

It should also be recognised that this element of the TSS is an important one because it is clearly linked to what we believe to be the rationale for network tariff reform in Queensland. We consider that network tariff reform is about conveying more cost reflective price signals to Retailers with the objective of incentivising the retail market to discover innovative ways of managing the risks created by reform. Providing a choice of cost reflective tariff structures will support this innovation process. It will also encourage retailers to provide a choice of cost reflective tariff structures to their customers, which is particularly important given concerns over the complexity of demand charges, as discussed in Section 18.4.1 of this final decision.

18.4.6 There is scope to improve the Queensland distributor's preferred methodology for LRMC estimation

While we accept on balance that the Queensland distributor's proposed LRMC estimation methodology is fit for purpose at this stage of tariff reform, we remain concerned over some aspects of the approach, as discussed in our draft TSS decision. We consider that the LRIC framework is appropriate in an environment of increasing demand and expenditure. While growth has historically been the typical scenario for an Australian distributor, we consider scenarios of stagnant or declining growth in demand for electricity distribution network services are more likely given the increasing penetration of DER and new technology. Rapidly developing technologies such as solar PV and battery storage, as well as more efficient appliances, could lower demand for network services. Changes in customer behaviour - which could be influenced by the transition towards more cost reflective tariffs, among other measures - may also trend towards more conservative demand for network services. We therefore consider that the Queensland distributors should also consider the implications of stagnant and declining demand growth in their LRMC estimation framework. This is particularly relevant for the Queensland distributors, where there is spare capacity.

We encourage the Queensland distributors to explore the inclusion of repex into LRMC calculations in such an environment. For example, the Queensland distributors could derive LRMC estimates by investigating the avoided costs of replacement with lower capacity assets in areas of declining demand. This is similar to the LRMC estimation methods of Endeavour Energy and Evoenergy.[54]

18.4.7 We support more research into capacity tariffs

The Queensland distributors propose to undertake a capacity tariff trial during the 2020–25 regulatory control period.[55] We support this element of the revised TSS given

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[54] For an example of such an approach, refer to link below: https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/endeavour-energy-determination-2019-24/proposal

[55] Ergon Energy, *Revised Tariff Structure Statement*, December 2019, p.5.

that it is consistent with our guidance in the draft TSS decision[56], which noted that the particular design of the capacity tariff in the initial TSS proposals raised serious concerns from both an efficiency and customer impact perspective. Stakeholders also expressed concern over the design of this tariff proposal.[57]

We consider that the best way to address our concerns is by working with stakeholders to test different capacity tariff designs. If well designed and executed, a tariff trial will also shed light on the following key issues, as summarised in the table below.

Table 3: Examples of key questions to be answered by capacity tariff trial

Key research question	Description
What is the intended role of the capacity charging parameter in the capacity tariff structure?	Is this charging parameter intend to achieve better economic outcomes? If yes, how does it play an economic purpose i.e is it to efficiently recover residual costs or to signal LRMC of peak capacity? Is this charging parameter intend to achieve equity outcomes eg. to reduce inherent cross subsidies by reallocating network costs toward customers with high and inelastic demand at times of network congestion?
What are the different options for designing the capacity charging parameter?	There are a plethora of design options available for the capacity charging parameter. For example the capacity value could be based on the individual customer's historical peak in half hourly maximum demand. Alternatively, the capacity value could be based on the individual customer's maximum demand at time of network congestion.
What is the inter-relationship between the capacity charge and other charging parameters in the capacity tariff structure?	The optimal design of the capacity tariff is likely to require a clear understanding of the role played by each charging parameter. For example if the capacity charging parameter is primarily designed to recover residual costs, there may be an argument for removing the fixed charge. Alternatively if the capacity charge is intend to signal LRMC of peak network capacity, there may be argument to remove peak energy charging parameters.
Is the capacity charging parameter the best way to achieve the intended outcomes	The capacity charging parameter is complex and likely to be difficult for many end customers to understand and respond to. Do the benefits outweigh the additional costs? Are there simpler tariff options that achieve a similar net benefit?
Will retailers pass through the network capacity charging parameter to end customers? To what extent will these decisions be influenced by the design of the capacity charging parameter and the preferences of end customers?	How will retailers respond to complex network price signals? Will they overlay these charges with simpler charging parameters and manage the underlying risk in some other way i.e. demand management? Will they reflect capacity charges in retail pricing offers? Will retailers allow end customers in this situation to voluntarily take-up alternative tariffs such as a simple consumption tariff or TOU energy tariffs? To what extent does tariff switching undermine the realisation of the benefits of capacity tariffs at a network level?

[56] AER, *Draft Decision - Ergon Energy distribution determination - Attachment 18 - TSS*, October 2019, pp.36-37.

[57] QCOSS and Etrog Consulting, *Submission on AER's draft decisions and Queensland distributors' revised proposals and TSS*, January 2020, p.18.

Key research question	Description
What is the distribution bill impact under different capacity tariff designs? To what extent are customers willing and able to mitigate this impact by changing their load profile	What types of customers are likely to receive a passive bill saving under a capacity tariff structure? What types of customers are likely to pay more under a capacity tariff structure? To what extent are these customers willing and able to mitigate this impact by changing their load profile? How can the Queensland distributors assist Retailers to help these customers manage the impacts? Will transitional arrangements assist these customers

Source: AER analysis

18.4.8 Large residential and small business customers must be assigned to separate network tariff from 1 July 2021

We are not satisfied that Queensland distributors' proposed pricing arrangements for residential and small business customers with basic metering that are assessed as having consumption above 100 MWh pa comply with the pricing principles in the NER. We note that some of these customers are likely to be embedded networks, rather than typical residential or small business customers. This raises concerns over the efficiency of these pricing arrangements given the potential risk that these customers will have load profiles that materially differ to other large customers with similar levels of annual consumption. This is an issue of growing importance in other jurisdictions.[58] Stakeholders also raised concerns over the pricing arrangements for these types of customers in the context of the broader issue of how to efficient price network services to embedded networks.[59] We also have concerns over Ergon Energy's practice of reassigning customers in this situation to a SAC large business demand tariff using inferred demand quantities and the associated risk of imposing unacceptable bill shocks on customer when they are eventually charged on actual demand quantities once they have a smart meter installed.

To address our concerns we require that the Queensland distributors introduce new network tariffs specifically for residential and small business customers with basic metering that are assessed as having consumption greater than 100 MWh pa. We recognise that it may be difficult for Queensland distributors to introduce these new tariffs on 1 July 2020 given the short time available to make the necessary changes to their billing system and related processes. We also recognise that the Queensland distributors require time to engage with retailers and impacted stakeholders prior to introduction. It is for this reason that we consider, on balance, that it is appropriate to delay the introduction of these new tariffs until 1 July 2021. It is the AER's intention that all residential and small business customers that are assessed by the Queensland

[58] To understand the potential extent of the differences in load profile between large residential customers and large business customers refer to the recent Ausgrid TSS amendment proposal. This document is available from: https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/ausgrid-determination-2019-24/updates

[59] Queensland Energy Users Network, *Submission on AER's draft decisions and Queensland distributors' revised proposals and TSS,* January 2020, p.16.

distributors as no longer satisfying the small customer classification threshold of 100 MWh pa[60] from 1 July 2021 will be reassigned to the applicable new tariff given the nature of their usage.

We require that the Queensland distributors propose a structure for these new tariffs as part of their 2021–22 pricing proposals and to demonstrate that the proposed design of these tariffs satisfy the pricing principles in the NER. We require that these tariffs be based on actual billable quantities, as opposed to the current practice of using inferred demand quantities given our concerns. We are not in principle opposed to the Queensland distributors adopting an inclining block structure for these new tariffs, so long as it can be demonstrated that such tariff structures are consistent with the pricing principles.

Given the potential growth in embedded networks in the residential customer segment in the future, we encourage the Queensland distributors to explore the broader issue of how best to efficiently price network services to embedded networks during the 2020–25 regulatory control period.

18.4.9 Legacy seasonal tariffs for CAC customers are to be offered on an opt-in basis after 30 June 2020

Ergon Energy propose to either grandfather or retire the existing seasonal tariffs applying to residential, small business and large business customers from 1 July 2020.[61]

We raised concerns in regard to this proposal in our draft TSS decision where we noted that the seasonal nature of these tariffs mean that they are reasonably cost reflective and raise no customer impact concerns if offered on an opt-in basis.[62]

We accept the Queensland distributor's arguments that the efficiency properties of these tariffs is diminished by the broad peak charging parameter and the inclusion of these tariffs even on an opt-in basis for residential and small business customers has the potential to create adverse transitional impacts in the future given the Queensland distributor's long-term intention to assign customers to a capacity tariff. Nevertheless, we are not satisfied that it is compliant with the pricing principles in the Rules to retire the legacy seasonal demand tariffs for eligible customers connected to Ergon Energy's high voltage and sub-transmission voltage levels of the electricity distribution network.

We note that there are some agricultural customers that predominantly use the electricity network outside the summer peak period. We are concerned that denying these types of customers the opportunity to choose a seasonal cost reflective tariff will

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60 A small customer is defined in the National Energy Retail Law (Queensland) Act 2014 as a residential or small business customer with annual energy consumption lower than the threshold determined in Section 7 of the National Energy Retail Regulations.

61 Ergon Energy, *Revised Tariff Structure Statement*, December 2019, pp.19-20.

62 AER, *Draft decision - Ergon Energy distribution determination - Attachment 18 - TSS*, October 2019, pp.29-30.

result in these customers paying more for their network services than is justified on an economic cost to serve basis. It is for this reason, together with our view that these tariffs are reasonably cost reflective, we have amended the revised TSS to allow customers in CAC tariff class to access the legacy seasonal demand tariffs from 1 July 2020 on an opt-in basis.

18.4.10 Changes have been made to the proposed eligibility criteria for the ICC tariff class tariff

The Queensland distributors proposed to expand the eligibility criteria for the ICC tariff class to allow more business customers connected at the higher voltage levels of the electricity distribution network the opportunity to voluntarily opt-in to an ICC tariff. We support this proposal in principle given that the locational nature of these tariff arrangements has the potential to result in these tariffs being more cost reflective than published tariffs.[63]

As set out in our draft decision, we were concerned over the inadequate and unclear description of this element of the proposed tariff structure statement.[64] To achieve compliance with the pricing principles in the Rules, we required that Ergon Energy address our concerns in their revised tariff structure statement. While we acknowledge the efforts made by the Queensland distributors to address these shortcomings, we are still not satisfied that our concerns have been addressed. As a result, we have amended this element of the proposed tariff structure statement to ensure compliance with the Rules. To reduce unnecessary transaction costs we have adopted the same eligibility criteria for the ICC tariff class across both Queensland distributors. We have also removed the proposed eligibility criteria relating to the equitable treatment of customers on the grounds that we are not satisfied that this proposed criteria complies with the pricing principles in the Rules.

18.4.11 The basis of Ergon Energy's non-standard ICC tariff proposal has been amended to comply with the NER

Ergon Energy propose to allow certain large customers at risk of disconnection or network bypass to voluntarily opt-in to a non-standard ICC network tariff from 1 July 2020.[65] While we accept this proposed approach in principle, we do not consider that it is able to be implemented in practice due to the difficulties associated with Ergon Energy undertaking a risk assessment of this nature. In particular, we note that it is difficult given the information asymmetries for a electricity distributor to disentangle the drivers of risk that are directly attributed to the network tariff arrangements of the

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63 A standard published tariff for large business customers are typically designed by an electricity distributor to the average cost to supply network services to customers assigned to this tariff, regardless of where these customers are located within the electricity network. ICC tariffs are typically design to reflect the cost of providing electricity distribution and transmission services to the customer's specific connection point.

64 AER, *Draft decision - Ergon Energy distribution determination - Attachment 18 - TSS*, October 2019, p.16.

65 Ergon Energy, *Revised Tariff Structure Statement*, December 2019, Appendix A.

customer from risks that relate to firm or industry specific issues.[66] It is for this reason that we do not approve this approach. Nevertheless we accept that the customer impact issues that Ergon Energy is trying to address with this proposal are real given the views expressed in several submissions.[67][68] It is clear from the analysis undertaken by the QCA that some large customers, such as those with high (and inelastic) peak demand and intermittent or seasonal energy consumption patterns could be exposed to unacceptable electricity bill increases as a consequence of being reassigned to a standard regulated retail tariff on 1 July 2021. We accept Ergon Energy's argument that this issue requires a customer impact mitigation measure. While we do not support the basis of the Ergon Energy proposal, we consider that allowing these customers (subject to satisfying the applicable eligibility criteria) to opt-in to a non-standard ICC tariff where the demand charge is transitioned to LRMC over a reasonable period has a number of advantages, including:

- There is a potential under these tariff arrangements for customers to receive a reduction in the transmission component of their network tariff if they are supplied via a transmission Connection Point that has a lower transmission charges compared to other parts of the Powerlink transmission network. This reduction in transmission component of their electricity network bill is justified on a cost to serve basis.
- The flexibility afforded to Ergon Energy under this approach is likely to result in the adoption of a transition DUoS price path for the demand charge that better reflects the localised network circumstances of the customer. In parts of the network that currently have substantial levels of excess capacity and are expected to experience little if any growth in peak demand over the medium to longer term, it is appropriate for Ergon Energy to adopt a longer period of transition to LRMC-based demand charges. In addition to the efficiency gains, this approach also has the benefit of providing customers in this circumstance with a longer time frame to adjust to more cost reflective peak price signals. It should also provide these customers with a reasonable degree of certainty over the annual movements in the level of the peak demand charges. This also supports the efforts of these customers to investigate the commercial viability of investing in peak demand management measures and plant and equipment upgrades.

We accept the other elements of Ergon Energy's proposal to address the customer impact for these users, such as the introduction of new controlled load tariffs. In addition, our requirement explain above about maintaining existing seasonal tariffs for

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66 While a similar prudent discount approach applies in electricity transmission, in that case, an assessment occurs for a very small number of very large electricity users which reduces the complexity and transactional costs of the assessment. In Ergon Energy's situation, this assessment may need to be applied to thousands of individual electricity users.

67 White Industries, *Submission on AER's draft decision and Ergon Energy's revised proposal and TSS*, January 2020.

68 Bundaberg Walkers Engineering, *Submission on AER's draft decision and Ergon Energy's revised proposal and TSS*, January 2020.

CAC customers provides an additional customer mitigation measure option for these users.

18.4.12 We have concerns over the efficiency properties of the proposed excess demand charge for large SAC customers

The Queensland distributors propose to have an excess demand charging parameter in their cost reflective tariff structure for certain large business customers from 1 July 2020.[69] The proposed excess demand charging parameter is designed to discourage customers from shifting their utilisation of the electricity network from the peak period to the off-peak period. We accept that there could be an economic rationale for applying this type of charging parameter in the situation where a specific customer or group of customers is expected to respond to static peak price signals in a manner that causes localised congestion occurring outside the existing peak charging window times. However, we are not satisfied that on the basis of the information set out in the TSS that this risk is material for the customers assigned to the tariffs that are proposed to include the excess demand charging parameter. This is an empirical issue. We encourage the Queensland distributors to research this issue as part of the next round of TSS proposals for the 2025–30 regulatory control period.

Despite the efficiency concerns over the excess demand charging parameter, we approve this element of the TSS on the condition that the DUoS price level applied to this charging parameter does not exceed 30 per cent of the applicable LRMC estimate during the 2020–25 regulatory control period.[70]

18.4.13 Legacy tariff arrangements

The Queensland distributors raised in their revised TSS proposals the possible existence of existing network tariffs that do not comply with their existing TSS.[71] We are pleased that the Queensland distributors raised this issue and have committed to working towards its resolution.

Given that this issue was raised late in the process, it has not been possible for the AER to resolve this issue as part of this final decision. As a consequence, we have decided that the most appropriate action to take is to require the Queensland distributors to complete a review of their network pricing and billing arrangements on a reasonable endeavours basis by no later than 31 December 2020. This review is to:

- Identify legacy tariffs and the number of customers on these tariffs.

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69 Energex already currently have excess demand charges in place, Ergon Energy proposes to introduce this charging parameter to achieve consistency across the two Queensland distributors.

70 Except where the Queensland distributors are able to demonstrate that a higher price level is required for customer impact mitigation reasons.

71 Energex 2019, *Revised Tariff Structure Statement*, Section 5.4, page 27, December

- Assess the extent that these customers have been over or under charged.
- To work with relevant stakeholders to develop a plan to address any historical billing over/under recoveries to the extent reasonable to do so.
- To mitigate the impact of reassigning these customers to an appropriate default network tariff in future.

Shortened forms

Shortened form	Extended form
AER	Australian Energy Regulator
distributor	distribution network service provider
DUoS	distribution use of system
NEM	National Electricity Market
NEO	National Electricity Objective
NER or the rules	National Electricity Rules
DNSP	Distribution network service provider
repex	replacement expenditure

Glossary of terms

Term	Interpretation
Anytime demand tariff	A tariff incorporating a demand charge where the demand charge measures the customer's maximum demand at any time (i.e. not limited to within a peak charging window).
Apparent power	See kVA
Connection Asset Customers	A Connection Asset Customer (CAC) is a connection that has a network coupling point at 66kV, 33kV, 22 kV, 11 kV and installed capacity above 1,000 kVA who are not assigned to the Individually Calculated Customer (ICC) tariff class.
CoAG Energy Council	The Council of Australian Governments Energy Council, the policymaking council for the electricity industry, comprised of federal and state (jurisdictional) governments.
Consumption tariff	A tariff that incorporates only a fixed charge and usage charge and where the usage charge is based on energy consumed (measured in kWh) during a billing cycle, and where the usage charge does not change based on when consumption occurs. Examples of consumption tariffs are flat tariffs, inclining block tariffs and declining block tariffs.
Cost reflective tariff	Consistent with the distribution pricing principles in the NER, a cost reflective distribution network tariff is a tariff that a distributor charges in respect of its provision of direct control services to a retail customer that reflects the distributor's efficient costs of providing those services to the retail customer. These efficient costs reflect the long run marginal cost of providing the service and contribute to the efficient recovery of residual costs.
Declining block tariff	A tariff in which the per unit price of energy decreases in steps as energy consumption increases past set thresholds.
Demand charge	A tariff component based on the maximum amount of electricity consumed by the customer (measured in kW, kVA or kVAr) over a designated time-period which may be reset after a specific period (e.g. at the end of a month or billing cycle). A demand charge could be incorporated into either an anytime demand tariff or a time-of-use demand tariff.
Demand tariff	A tariff that incorporates a demand charge component.
Fixed charge	A tariff component based on a fixed dollar amount per day that customers must pay to be connected to the network.
Flat tariff	A tariff based on a per unit usage charge (measured in kWh) that does not change regardless of how much electricity is consumed or when consumption occurs.
Flat usage charge	A per unit usage charge that does not change regardless of how much electricity is consumed or when consumption occurs.
Inclining block tariff	A tariff in which the per unit price of energy increases in steps as energy consumption increases past set thresholds.
Individually Calculated Customers	An Individually Calculated Customer (ICC) is a connection that has a network coupling point at 132kV, 110kV, 66kV, 33kV that is assessed by the Queensland distributors as satisfying the eligibility criteria for the ICC tariff class.
Interval, smart and advanced meters	Used to refer to meters capable of measuring electricity usage in specific time intervals and enabling tariffs that can vary by time of day.
kVA	Also called apparent power. A kilovolt-ampere (kVA) is 1000 volt-amperes. Apparent power is a measure of the current and voltage and will differ from real

Term	Interpretation
	power when the current and voltage are not in phase.
kW	Also called real power. A kilowatt (kW) is 1000 watts. Electrical power is measured in watts (W). In a unity power system the wattage is equal to the voltage times the current.
kWh	A kilowatt hour is a unit of energy equivalent to one kilowatt (1 kW) of power used for one hour.
LRMC	Long Run Marginal Cost. Defined in the National Electricity Rules as follows: *"the cost of an incremental change in demand for direct control services provided by a Distribution Network Service Provider over a period of time in which all factors of production required to provide those direct control services can be varied".*
Minimum demand charge	Where a customer is charged for a minimum level of demand during the billing period, irrespective of whether their actual demand reaches that level.
NEO	The National Electricity Objective, defined in the National Electricity Law as follows: *"to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to—* *(a) price, quality, safety, reliability and security of supply of electricity; and* *(b) the reliability, safety and security of the national electricity system".*
Power factor	The power factor is the ratio of real power to apparent power (kW divided by kVA).
Tariff	The network tariff that is charged to the customer's retailer (or in limited circumstances, charged directly to large customers) for use of an electricity network. A single tariff may comprise one or more separate charges, or components.
Tariff charging parameter	The manner in which a tariff component, or charge, is determined (e.g. a fixed charge is a fixed dollar amount per day).
Tariff class	A class of retail customers for one or more direct control services who are subject to a particular tariff or particular tariffs.
Tariff structure	Tariff structure is the shape, form or design of a tariff, including its different components (charges) and how they may interact.
Time-of-use demand tariff (ToU demand tariff)	A tariff incorporating a demand charge where the demand charge measures the customer's maximum demand during a peak charging window. A ToU demand charge might also include an off-peak demand change or minimum demand charge, and may include flat, block or time-of-use energy usage charges.
Time-of-use energy tariff (ToU energy tariff)	A tariff incorporating usage charges with varying levels applicable at different times of the day or week. A ToU energy tariff will have defined charging windows in which these different usage charges apply. These charging windows might be labelled the 'peak' window, 'shoulder' window, and 'off-peak' window.
Usage charge	A tariff component based on energy consumed (measured in kWh). Usage charges may be flat, inclining with consumption, declining with consumption, variable depending on the time at which consumption occurs, or some combination of these.