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National Electricity Market Campaign

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Submission to AEMC

Economic Regulation of NSPs

Directions Paper

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Total Environment Centre's National Electricity Market Campaign

Established in 1972 by pioneers of the Australian environmental movement, Total Environment Centre (TEC) is a veteran of more than 100 successful campaigns. For the last forty years we have been working to protect this country's natural and urban environments: flagging the issues, driving debate, supporting community activism and pushing for better environmental policy and practice.

TEC has been involved in National Electricity Market (NEM) advocacy for eight years, arguing for greater utilisation of energy efficiency and demand side participation to meet Australia's electricity needs.

TEC's Position on the Economic Regulation of Service Providers

TEC welcomes the opportunity to provide further comment as part of the rule change process regarding the economic regulation of Network Service Providers (NSPs). TEC is of the opinion that the current regulatory framework of the NEM systemically favours the supply side and encourages greater capital expenditure on infrastructure (capex) at the expense of DSP solutions to meeting demand for electricity.

In our submission to the AEMC's Issues Paper, we outlined in detail our position in relation to the proposed changes to the economic regulation of NSPs. We consider that weak economic regulation is a significant part of the supply-side bias in the NEM as it heavily favours NSPs and disadvantages the Australian Energy Regulator (AER), which has found it difficult to curtail excessive capex. This has resulted in increased prices for consumers beyond those necessary to achieve an efficient, safe and reliable electricity supply.

Our position remains unchanged: these rule change proposals seek to address this part of the supply-side bias in the NEM and TEC is therefore broadly supportive. These rule changes will assist in curbing spiralling network costs and electricity prices. Nonetheless, more will be needed, including a shift in the mindset of the NEM's regulatory institutions and the National Electricity Rules to focus on the future of our energy system: distributed generation and demand-side participation.

Response to the Directions Paper

TEC is concerned that the Directions Paper is not heading in the right direction. The changes proposed by the EUC and the AER have the potential to significantly reduce electricity prices and also ensure that consumers are not forced to bear the high costs of weak regulation.

As we noted in our previous submission, it is unsurprising that NSPs are against this proposal. However, the AEMC must press on with important reform, even if this is unpopular this may be with the monopoly businesses that profit greatly from weakness in the current rule.

TEC, as well as other organisations, see these rule changes as some of the most important since the inception of the NEM, and as part of a broader move toward a more functional, efficient and progressive energy system. This can be seen in the range of reviews currently taking place and the broad public support for change in the NEM. The AEMC has a pivotal role to play in ensuring efficient provision of network services and fair prices, particularly in facilitating this rule change.

In our issues paper submission we argued that:

1. The AER should be given wide flexibility in its decision-making;
2. The limited merits review process requires reform as it hinders the AER's discretion;
3. The WACC and rate of return are amenable to being defined by a rule from the outset and this should be the case;
4. NSP profits are manifestly excessive;
5. Government-owned companies are able to leverage a superior credit rating to obtain finance at a much more advantageous rate: this should be accounted for in WACC determinations.

We remain adamant that these changes are necessary, and make the following comments in relation to the Directions Paper specifically:

1. The rate of return calculation is amenable to specification in the Rules and should be so specified. As previously noted, by TEC and others, this will promote certainty and simplify the regulatory process.

2. We do not agree with the rejection of suggestion that the return on debt for government-owned NSPs should be related to the cost of debt to the jurisdictional governments.

3. The onus of proof that regulatory expenditure allowances are efficient should rest with the NSP that proposes the expenditure, whereas at present this onus is on the AER. This is of paramount importance in shifting the balance back from being heavily in favour of NSPs. This also happens to be one of the simplest parts of these rule change proposals. As such, TEC can see no reason for the AEMC not to implement this change.

4. Efficiency incentives need to be significantly strengthened. In many other jurisdictions the focus of network regulation is on incentivising efficient and innovative behaviour on the part of NSPs. In Australia the Regulator is always ‘on the back foot’ trying to fight unrealistically lofty capex proposals. Again, the balance needs to be shifted.

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