



Total Factor Productivity for Distribution Network Regulation Rule Change Proposal – Section 108A Report

Purpose

The Australian Energy Market Commission (Commission) is required under section 108A of the National Electricity Law (NEL) to publicly report on Rules not made within 12 months of publication of the notification of the commencement of the Rule change process.

Background

On the 23 June 2008, the Victorian Minister for Energy and Resources submitted a proposal to amend the National Electricity Rules (Rules) to allow the use of a Total Factor Productivity (TFP) methodology as an alternative economic regulation methodology to be applied by the Australian Energy Regulator (AER) in approving, or amending, determinations for electricity distribution service providers.

Following this request, on 24 July 2008, the Commission published a notice under section 95 of the NEL advising of its intention to commence the Rule change process and initial consideration on the TFP for Distribution Network Regulation Rule Change Proposal (TFP Rule Change Proposal).

Reason for the final Rule determination not being made within 12 months

The reason why the Rule determination has not been made within 12 months of the publication of the notice under section 95 of the NEL is because consideration of the TFP Rule Change Proposal has been postponed to allow for a wider review of TFP to be carried out (TFP Review).¹

Once the TFP Review is complete, the Rule Change Proposal process will resume in respect of the TFP Rule Change Proposal. Some relevant background on the TFP Review is set out below.

Expected time for making final Rule determination

It is anticipated that the TFP Review will be completed by June 2010.

The Commission considers it will make and publish the final Rule determination for the TFP Rule Change Proposal by 31 December 2010.

TFP Review

Following consideration of submissions received in the initial round of consultation, the Commission decided to undertake a wider review into the possible use of TFP into revenue and pricing determinations for electricity and gas service providers (TFP Review). The TFP Review, which commenced on 21 November 2008, will enable the Commission thoroughly to consider and analyse the complex issues involved in assessing the use of TFP. Following completion of the TFP

¹ On 23 July 2009, the Commission published a notice under section 107 of the NEL extending the time for publication of a draft Rule determination in respect of the TFP Rule Change Proposal to 1 October 2010. This was to take into account its revised timeline for completion of the TFP Review.

Review, the Commission will be in an informed position to undertake an assessment of the TFP Rule Change Proposal.

The TFP Review is seeking to provide advice to the Ministerial Council of Energy (MCE) on:

- the circumstances in which an application of a TFP based price setting methodology would contribute to the National Electricity Law Objective (NEO) and National Gas Law Objective (NGO);
- the arrangements (including information, reporting and data requirements) that need to be put in place to facilitate its application; and
- as appropriate, the development of proposed Rules to support the applications of a TFP based form of control for any individual or group of electricity or gas distribution or transmission service providers.

The Commission is adopting a staged approach to addressing the question of whether TFP should be used in pricing and revenue decisions. First, the Commission will make an assessment of whether it considers that a TFP methodology would promote either the NEO and/or NGO and therefore should have a role in the relevant decision making processes. In doing so, the Commission will look at the possible range of models for applying TFP and will assess a number of issues relevant to the TFP Rule Change Proposal. At the end of this stage, the Commission will provide its findings to the MCE for its consideration (Stage 1 Report).

If the Commission considers that Rules should be made to facilitate the use of a TFP based methodology for either, or both, gas decisions or electricity determinations, it will then proceed to develop its recommended draft Rules to be submitted to the MCE (Stage 2 Report).

It is anticipated that Stage 1 of the TFP Review will be completed by April 2010. If required, Stage 2 of the TFP Review will be completed by June 2010. At this time the Commission will be in a position to resume consideration of the TFP Rule Change Proposal in the light of its findings as part of the TFP Review.