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Australian Energy Market Commission
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By email: submissions@aemc.gov.au

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Dear Madam/Sir

Transmission Pricing Issues Paper

The following comments are submitted in response to the AEMC *Transmission Pricing : Issues Paper*. The very broad nature of the questions raised in the paper have made it difficult for PIAC to allocate the resources needed for a more detailed response. This is particularly the case in the current environment of a high level of 'consultation' around national energy market issues. Nonetheless, PIAC remains keenly interested in these issues and the likely future approach to network pricing.

In particular, we wish to comment on the proposition on page 15 of the *Issues Paper* that longer term outcomes should be given 'due weight' in decisions on network pricing. PIAC agrees wholeheartedly that the longer term outcomes should be considered, particularly in relation to consumer benefit. Our view has been that the public interest is best served by taking account of the longer term needs and interests of end-users, especially residential consumers. It is a concern, however, that some may hold the view that consumer benefit somehow is linked to prices 'below their long run economic cost' – as if calls for consumer benefit rely only on demands for 'cheap' energy.

The task in relation to delivering consumer benefit requires a balancing not only of short and longer term outcomes but also of the needs of consumers for a supply of energy which remains both of appropriate quality and affordable. Put simply, the best functioning market (judged perhaps by efficiency and levels of investment) will be of little use to consumers who are 'priced-out' by charges beyond what they can pay. Nor is it enough to rely on a market response from consumers to achieve an appropriate balance between the supply side and the interests of end-users. The fact that energy is an essential service precludes such an approach from the perspective of both economic theory and social policy.

PIAC believes the onus should be on those making proposals for more dynamic and efficient energy markets to demonstrate how these will benefit consumers in each case. The possible introduction of more widespread use of interval meters is one example. Decisions to use traditional investment in physical assets over options for demand management are another. It is not enough simply for the network providers to cite 'efficiency' or 'investment' as if these outcomes can be relied on to bring net benefits to all consumers.

Following from these points we wish to give our support to the option proposed in the *Issues Paper* (page 31) of approaches to network pricing which seek to achieve both economic efficiency and social equity. Since the long term public interest is served by appropriate prices for network services PIAC acknowledges that price rises will be required from time-to-time. The question is whether these can be achieved with little or no negative social impact.

Economic efficiency and social equity do not always have to be mutually exclusive. However, the desirable approach to network pricing is one which is able to balance these sometimes divergent goals. In Australia, community and consumer groups repeatedly have voiced their desire for a national market which provides consumers with continuous access to an affordable, reliable and safe supply of energy. This is to be seen as applying to all consumers and not only those with the financial wherewithal to benefit from participation in a competitive energy market. The true test of a market in essential services is the extent to which it can meet the needs of the weakest consumer. Accordingly, consumer benefit cannot be measured by outcomes which direct the gains at a minority of consumers or which create a rump of households who can remain in the market only through taxpayer funded bailouts.

We take a similar approach to the question of whether pricing methodologies for energy networks should be based on LRMC approaches or those which emphasis short-run costs. The *Issues Paper* compares these approaches in relation to the way they treat different measures of 'efficiency'. PIAC does not question the validity of either of the arguments for short term or long term efficiency. However, we believe that a debate on these terms omits any consideration of the public interest and what approach provides the best outcome for household users of energy.

Given our support for economic regulation which addresses equity both between and within customer classes PIAC considers that LRMC approaches to network pricing provide the better match between the interests of network providers and end-users. It is pointed out to us repeatedly that a key to the proper functioning of an energy market is appropriate and timely investment in capacity. Pricing based on long-run investment decisions should meet consumer needs in terms of security of future supply and satisfy the demand that this be provided in a manner which all consumers can afford. Since LRMC approaches recognise the long life of network assets, prices derived in this way should balance the 'lumpy' nature of network investment meaning less volatile prices and less risk of price shocks for consumers.

Finally, section 7.2.2.1 of the *Issues Paper* notes the proposal that the network businesses should be able to decide which of the marginal cost approaches to apply to their specific networks. In our previous comments to the AEMC on the economic regulation of energy networks PIAC has expressed support for some regulatory discretion. We wish to make it clear this is intended to apply to the regulator and not to the regulated businesses. That is, while we think it unwise for too many statutory constraints to be placed on regulatory decision making we do not support a wide discretion to be granted to monopoly network providers.

Even the largest energy users can have difficulty engaging with the network operators in seeking appropriate pricing outcomes. What we have observed in NSW is that the discretion allowed by the regulator provides little real check that the pricing decisions of the distribution businesses are achieving the best balance of the needs of consumers beyond that established by side constraints. If a case can be made that different methodologies are appropriate to be used for different networks or pricing of different assets PIAC believes strongly this should be a matter for determination by the regulator.

Yours sincerely
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