

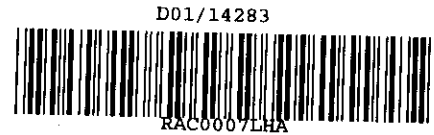



Queensland
Government

Treasury

- 3 MAY 2001

Mr R Shogren
Commissioner
Australian Competition and Consumer Commission
PO Box 1199
DICKSON ACT 2602



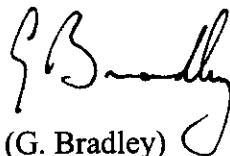

Dear Mr Shogren

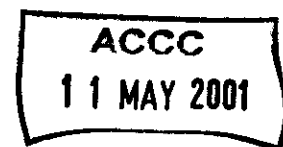
Submission on ACCC Network Pricing and Market Network Service Providers Draft Determination

Please find enclosed the Queensland Government submission in response to the ACCC Network Pricing and Market Network Service Providers Draft Determination.

Queensland Treasury would be happy to discuss its comments with the ACCC and you are invited to contact Mr Alan Tesch, Executive Director, Office of Energy on (07) 3224 5378 should you wish to take up this offer.

Yours sincerely


(G. Bradley)
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**Queensland
Government**

Treasury

ACCC Draft Determination

Application for Authorisation

**Amendments to the National Electricity
Code**

**“Network pricing and market network
service providers”**

Queensland Government Response

Opening remarks

The Queensland Government (Queensland) appreciates the opportunity to comment on the ACCC's draft determination in relation to "Network Pricing and Market Network Service Providers".

Queensland recognises the current market design of the NEM is not perfect and that there is the potential for consumer benefits through improvements as the NEM matures.

Queensland will only support changes in the NEM design where these improvements have been robustly assessed, against the existing NEM design, and proven to deliver price and/or other tangible benefits to consumers. Development of the NEM should only be undertaken where the reforms can be readily implemented and managed by NEM participants without adverse consequences for consumers.

Queensland does not support aspects of the Draft Determination

Queensland has a number of fundamental concerns with the proposed draft determination and, in particular, the proposed system of transmission usage charges and the conditions of authorisation relating to those charges. Queensland also has concerns with the ACCC's comments in relation to Distribution Network Pricing, Information Disclosure, Embedded Generation and Market Network Service Providers.

Transmission Network Pricing

Queensland is principally concerned that there are a number of current reviews and recent determinations which seek to improve locational investment signals by either financial incentives (eg. embedded generation transmission rebates), price signalling (eg. RIEMNS, VoLL increases) or by improving cost reflectivity (eg. certain aspects of this determination).

To date, these reviews have taken a piecemeal approach to NEM development and have not sought to take the NEM forward in a coordinated way. Importantly, none of these reviews have sought to robustly assess and quantify the short term and long term net benefits from the proposed changes. Indeed, to date these reviews have arguably concentrated on an idealistic approach to NEM development rather than focussing on realistic and practical outcomes.

What is also evident is that the impact of these recommendations has not been the subject of any quantitative analysis that assesses the combined impact of the proposals in this determination and other proposed changes in NEM design, to determine the incremental net benefits from each step change in NEM design. Moreover, when that analysis has been attempted, the results have been flawed because they have not robustly assessed the net benefits of the proposed changes in the NEM (eg. NECA's analysis in the RIEMNS review).

Queensland is concerned that unless there is a coordinated approach to NEM development which concentrates on the short and longer term net benefits to end users, as opposed to solely long term theoretical economic efficiency, then there is potential that the benefits of the NEM may be compromised.

With regards to the ACCC's draft determination, Queensland notes that in developing the proposed amendments to the Code changes, the ACCC has not sought to quantify the market impacts of their proposals or determine the workability of the revised Code changes. Indeed, the ACCC has undertaken no quantitative analysis to support the claimed benefits of their proposals.

It is with interest then that Queensland notes the analysis tabled by NECA at the pre-determination conference. This analysis highlights the volatility and unintended price outcomes of the ACCC's proposals. On this basis, Queensland questions whether there is a net public benefit by adopting the ACCC's proposed methodology.

In this respect, Queensland submits that a number of the ACCC's proposals:

- are fundamentally different from the code changes submitted by NECA;
- fundamentally alter the NEM design;
- have been developed in isolation of other proposed NEM improvements to locational price signalling;
- have not been the subject of a rigorous consultation in their development; and
- the benefits of the proposals have not been adequately assessed or quantified.

Queensland is concerned that the ACCC is considering authorising code changes when the benefits and impacts of these proposed changes have not been, and arguably in their present form cannot be, quantified or qualitatively assessed.

Queensland is also concerned that the ACCC proposes to authorise Code changes, including conditions of authorisation before a robust methodology underlying the Code changes has been developed.

Whilst it is arguable that the ACCC has sought to address this deficiency by requiring NECA to develop and consult on a methodology for transmission pricing that meets the ACCC's guiding principles, this process falls short of the normal process for development of code changes and is unsatisfactory. It is also unsatisfactory that the ACCC has sought to adopt a greater policy role in developing these proposals when that role arguably falls with jurisdictions and to a lesser extent with NECA.

In summary, the ACCC should note that from Queensland's perspective:

- the proposed code changes contained in the conditions of authorisation are ambiguous and are open to a range of interpretations. Queensland is also concerned that the proposed Code changes may prove undeliverable in a practical sense. Queensland is concerned that this could lead to uncertainty for market participants and to legal disputes if the Code requirements cannot be met;
- the proposed changes could lead to financial flows across the NEM that have not been quantified. This may have a consequential financial impact on Queensland customers and, on the Queensland Government (if tariff support is necessary) and on market participants;
- the proposed changes could lead to changes in the relative cost structures of generators which could impact on bidding behaviour and wholesale electricity pool prices. Combined with the variability in usage charges this would increase price volatility and retailer financial risks. This risk will ultimately be borne by customers in the form of higher prices. As a result of the lack of analysis and ambiguity in the draft determination, Queensland is unable to determine the price impacts and risk management issues for Queensland consumers and market participants;

- the validity of a number of the ACCC's assumptions that have led to the conditions of authorisation has not been assessed. This could lead to transmission usage charges not achieving their intended outcome of relieving congestion and promoting efficient network and generation investment. An example of this is the assumption that loads will react to time/price and location signals. However, sending these price signals to smaller customers and some larger customers may not lead to changed consumption patterns or location because those customers are price takers and individually are of insufficient size to materially affect network congestion/energy demand at a given point in time. Moreover, with the existing metering technology, these price signals cannot be practical sent because time of use data is not available.

Alternatively, in the case of generation, the ACCC must recognise that there are other factors (eg. environmental constraints and fuel availability) which may limit the ability of generation to locate in areas with low local generation capability;

- the ACCC's proposed Code changes appear to steer the NEM towards a nodal pricing system via the use of time and location variable transmission usage pricing. Queensland notes that other reviews have examined the introduction of nodal pricing in the NEM (ie. NECA's RIEMNS review) and concluded that it could not be implemented with positive effect; and
- a "holistic" approach to the development of transmission pricing and locational signalling in the market is needed. Accordingly, Queensland does not support the authorisation of Code changes in relation to the transmission usage charges contained in the draft determination because they have been developed in isolation of other proposed Code changes that also seek to improve locational price signals.

On this basis, Queensland recommends that the draft determination in relation to transmission pricing not be finalised in its current form and that more meaningful assessment be carried out. There should be no final determination and:

- The ACCC should refer the issue of network pricing and market network service providers back to NECA and the jurisdictions to develop a revised transmission policy that integrates the proposals arising from the RIEMNS review as well as other relevant issues in the network pricing debate (eg. firm access rights);
- NECA be required to develop Code changes that recognise the legitimate reform requirements of the NEM jurisdictions; and
- NECA and the jurisdictions develop an integrated coordinated timetable for development and implementation of this "holistic" market reform package.

Additional Specific Comments on Transmission Pricing

ACCC conditions of authorisation in relation to transmission pricing

Amendments to the Code (C4.1)

Subsection 3 and 5

The ACCC has determined that transmission usage charges at a particular location and time should reflect the likely impact that an increase in the local off-take would have on network congestion.

Queensland is concerned that this could be interpreted to require that transmission usage charges adopt a methodology that varies with usage in a manner akin to nodal pricing. Queensland does not draw this conclusion from the examples contained in Appendix C to the draft determination. Irrespective of this, the guiding principles in the draft determination are not sufficiently clear to rule out the development of this arrangement, particularly given the ACCC's stated preferences for nodal pricing.

Queensland notes that NECA has, through the RIEMNS report, rejected the adoption of nodal pricing in the NEM and would be concerned that an arrangement akin to nodal pricing could arise in the NEM. Queensland is particularly concerned that nodal pricing might be achieved through the transmission network when this arrangement is best implemented via the wholesale energy market.

Queensland recommends that the ACCC improve the clarity of this objective to remove ambiguity in relation to nodal pricing by removing the wording from principle C.4.1.3 "at the time usage occurs" and from principle c.4.1.5 "at a particular time and location".

Amendments to the Code (C4.2)

The NECA process

It is noted that the ACCC has required NECA to develop, model and test a default pricing methodology that satisfies the principles contained at C4.1 of the Conditions of Authorisation. This process is to be conducted in accordance with Code consultation processes. A timeframe of twelve months has been provided for this process.

Queensland raises a concern that this timeframe is not sufficient to allow a robust process to occur. Any process to develop revised transmission price outcomes must:

- develop all possible alternatives and consult to determine whether other alternatives exist;
- qualitatively and quantitatively assess the incremental impact on market outcomes from each of the proposed alternatives, including assessment of impacts on the wholesale electricity market and synthetic markets, impacts on delivered energy prices, the impacts on market participants and potential generation and transmission investments; and
- consult widely on the selected pricing methodology and the outcomes of analysis that support the proposed methodology; and
- develop code changes for ACCC approval.

Queensland is concerned that the appropriate consultation will be compromised by this timeframe and the opportunity for market participants and jurisdictions to assess and influence the outcomes of NECA's process could be impeded if the current timeframe is strictly adhered to. Queensland recommends that a timeframe of 18-24 months would be more appropriate.

Queensland notes that it is not clear from the condition of authorisation whether the proposed methodology developed by NECA is to result in Code changes. Given that transmission pricing is presently codified, Treasury would expect that revisions to the Code would result from the C4.2 process.

Queensland recommends that the ACCC clarify this position.

Distribution Network Pricing

It is Queensland's view that distribution pricing is a matter for jurisdictional regulators and that this was the original intention of the Code and Queensland does not support any move by the ACCC to codify the principles of distribution pricing as it is unlikely that the legitimate policy interests of individual NEM jurisdictions will be able to be met on a national basis.

Queensland notes that the ACCC seeks to amend the Code to require that the structure of DUoS charges be refined to enable location and time signals of the proposed transmission pricing regime to be fully passed through to consumers. However, Queensland notes that franchise tariff customers in Queensland currently do not receive locational and time/price signals due to the structure of the franchise tariff arrangements. Moreover, in relation to time/price signals, Queensland notes that for customers who do not have interval meters these signals cannot be provided other than through profiling. However, profiling does not reward the smaller customer for reacting time/price signals and charging consumption accordingly. Therefore, there is questionable benefit to be realised from requiring these signals to be preserved in distribution prices. In the event interval meters were available to small customers, Queensland questions whether there is sufficient elasticity in their demand that they will change consumption patterns as a result of time/price signals. That is, most small consumers are likely to treat electricity as an essential service and will therefore show only limited reaction to price signals.

On this basis, Queensland submits that providing locational and time/price signals to smaller customers is unlikely to result in changed consumption patterns and is, therefore, unlikely to result in significant public benefit through ultimately, more efficient network investment.

Queensland, therefore, does not support this recommendation and requests that the ACCC remove the requirement for DUoS to reflect transmission pricing signals from the final determination.

Network Planning and Augmentation

Development of networks in a region

Queensland makes no comment on this section of the draft determination.

New investments – beneficiary pays

Queensland notes that NECA has developed a revised framework in relation to the beneficiary pays proposals and, given that the ACCC in its draft determination has sought to delay consideration of this issue until the revised arrangements are developed, makes no comments on this issue at this point in time but reserves the right to comment in future.

Information disclosure

Unbundling TUoS usage and general charges

Queensland makes no comments on this section of the determination.

Unbundling TUoS and DUoS charges

Queensland does not support the unbundling of TUoS and DUoS for franchise tariffs in Queensland. For smaller customers to whom contestability is not yet an option, the disaggregation of these tariffs at this point does not provide any net benefits. Further, provision of this information for smaller customers will increase costs in Queensland without

any benefits. Ultimately, these costs would lead to increased tariffs prices for consumers or to increases in the Government subsidy identified above.

Only if and when a form of congestion based network pricing is introduced will the disaggregated information prove to be of financial benefit to smaller consumers. However, the provision of this information at this time does not allow these customers to act to achieve financial reward by altering their usage.

Queensland notes that its position not to disaggregate DUoS and TUoS information will not impact on the provision of this information to those large franchise customers (>200MW pa) who are able to choose contestable terms. This is because DUoS and TUoS charges are already published in Queensland for these customers and this arrangement allows these customers to examine the financial merits of contestable prices against franchise prices and, therefore, achieves the same outcome that the ACCC is seeking.

On this basis, Queensland recommends that the ACCC only extend the policy of disaggregating DUoS and TUoS prices to customers who are contestable or eligible to take contestable terms.

Service standards, negotiable services and access services

Queensland makes no comments on the ACCC findings and decisions in this component of the draft determination. Queensland does submit, as raised earlier in this submission, that there is a need for a review of the operation and negotiation of firm access rights as part of the development of a revised network pricing arrangement.

Any arrangement for firm access rights must recognise that the provision of and costs associated with firm access are additional to transmission costs that should be levied on generators. In addition, any regulatory structure must be flexible enough to reward NSP's for the financial risks associated with providing firm access rights. In that regard, it is noted that the current regulatory revenue cap process places incentives that do not facilitate or reward NSPs to negotiate firm access.

Embedded Generation

Queensland notes the intention to pay embedded generators a transmission savings rebate. Queensland only supports this policy where those rebates do not exceed the loss savings actually obtained by the organisation making the rebate and where the embedded generator is required to bear the full costs of connection, including upgrade costs to the distribution network and other network assets (eg. sub-stations etc.).

It is Queensland's view that if this policy is to be adopted then there is a need for improved clarity in relation to eligibility. There is a need for the eligibility to be limited by placing restrictions on generator size and for tightening of distribution network definitions (refer to Powerlink and Vencorp's concerns raised at page 89 of the draft determination). Queensland notes that whilst the ACCC agreed the need for a limitation on the size of embedded generation eligible to receive transmission avoidance rebates, the draft determination make no decision on such a size limitation.

Placing constraints on embedded generation size is important for two reasons:

- it ensures that there are no perverse investment incentives placed on large generators to embed in the distribution network; and

- it minimises the financial consequences to other customers of the TNSP as a result of the TUoS rebates.¹

It is noted that there are presently a number of different definitions of embedded generation. Therefore, if the Code is to be amended to provide a financial incentive for generation to embed within the distribution network then there is a greater need for clarity of embedded generation and the eligibility for transmission avoidance rebates. If large scale generation was to be classified as embedded generation, there could be significant financial implications for TNSPs, market participants and for customers.

Queensland, therefore, recommends that an appropriate definition of embedded generation should be adopted which limits the size of embedded generation eligible for transmission avoidance rebates to generation of no more than 30MW capacity.

Queensland also supports the need for these rebates to be subject to some form of availability commitments and performance requirements placed on the embedded generator. This is because the reliance on embedded generation by Network Service Providers (NSPs) to maintain supply can lead to lower network investment and thereby reduce capacity of the network to meet increased demand in times when the embedded generator is unavailable. As NSPs remain responsible for the reliability of their network, increased embedded generation results in reliability of supply for the NSP being potentially compromised as a result of the trade-off between network investment (and the risk of optimisation of excess network investment) and the need to supply energy within the distribution network when the embedded generator is unavailable.

It is therefore appropriate that, to some degree, embedded generators should be held accountable for their availability particularly in times of peak demand. Therefore, Queensland recommends that the appropriate body should institute some form of availability commitments and performance requirements to which payment of the rebates is linked. These criteria should be reflective of consumption patterns in the distribution area and ensure that the loss savings are actually achieved. In addition to financial benefits there should also be a regime of penalties for failing to meet availability commitments and performance requirements.

It is Queensland's view that its proposed changes will still provide advantages to embedded generators over transmission connected generators. This is because, when compared to transmission connected generators, embedded generators receive a reward for lowering loss factors within the region that it is connected.

Market Network Service Providers

Queensland supports the safe harbour provisions for MNSPs and agrees with the ACCC's conclusions on the safe harbour provisions.

Queensland agrees that there is a need to ensure that there is equitable treatment between all market participants. On this basis, whilst Queensland agrees with the ACCC's comments that there should be equality between MNSPs and embedded generators in terms of transmission usage rebates, similar to embedded generators, these should be limited to MNSPs below a threshold size. For equity reasons, Queensland would support a recommended size limitation of 30MW for MNSPs to be eligible for transmission usage saving rebates. In making this recommendation, Queensland notes that the safe harbour

¹ As TNSPs receive a fixed revenue cap any revenue reduction resulting from lower loads on the transmission network are effectively recovered by higher prices to other customers across the transmission network which remove the under recovery. The situation is similar when DNSPs are required to pay the transmission usage rebates with the exception that the costs are limited to customers within that DNSPs distribution network.

provisions limit minimum MNSP capacity to 30MVA and, therefore, only a limited number of MNSPs will meet the eligibility requirements for transmission usage savings rebates. However, Queensland maintains support for its proposed limits on equity grounds.

Queensland supports the ACCC's view that there should be equitable treatment between MNSPs and other market participants (where MNSPs are acting as market participants) and between MNSPs and regulated network services. In that vein, Queensland supports the view of the ACCC in respect of levying TUoS on MNSPs. Queensland does not support the ACCC's proposed approach to transmission usage charges, Queensland's view is that the development of any new arrangement must ensure that MNSPs pay transmission network charges where applicable.

Given the likely delay in finalising revised transmission pricing arrangements, Queensland notes that there is a need to determine an approach that ensures equity in the interim. In this regard, the existing arrangements need to be updated to ensure that MNSPs pay TUoS where they act as a load. The ACCC should address this issue in its final determination.

In relation to network augmentation, it is important that MNSP's and embedded generators, similar to generators, are required to bear the costs of network augmentation that arises from the connection to the network. This is particularly important when it is considered that embedded and transmission connected MNSP's can result in both high cost augmentation in the distribution network as well as lead to transmission network augmentation (if the MNSP acts to increase congestion on the transmission grid). By way of example, the operation of Directlink when power flows south to Mullumbimby leads to increased incidences of network constraint along the transmission lines from the Brisbane area to the Gold Coast. As a result, augmentation of this network is required, the costs of which if it is not borne by Directlink, it would be unfairly borne solely by customers in Queensland (where the transmission and distribution upgrades are required) irrespective that both NSW and Queensland customers can benefit from the MNSPs existence.