

Brisbane Office

Ref:

30 September 1999

Mr Hank Spier
Chief Executive Officer
Australian Competition and Consumer Commission
PO Box 1199
Dickson ACT 2602

Dear Mr Spier

Submission on Transmission and Distribution Network Pricing Issues

Stanwell Corporation appreciates the opportunity to contribute towards the development of transmission and distribution network pricing framework and has prepared the attached submission in response to the ACCC's issues paper on National Electricity Code network pricing code changes of September 1999.

Yours sincerely

P Simshauser
TRADING MANAGER

Encl:

Enquiries: Kuan Chia
 Telephone 07 3335 7467
 Fax 07 3335 7477

STANWELL CORPORATION

A.C.N. 078 848 674

Submission to the Australian Competition and Consumer Commission on Transmission and Distribution Network Pricing Issues

September 1999

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Introduction

Stanwell Corporation Limited (SCL) appreciates the opportunity to make a submission to the Australian Competition and Consumer Commission (ACCC) in respect of transmission and distribution network pricing issues.

SCL is committed to providing competitive generation options to the market. Transmission and distribution network pricing issues are therefore of major interest to SCL as network charges have a significant impact on the financial viability of SCL's generation projects.

SCL views on transmission and distribution network pricing

SCL supports the general thrust of the National Generator Forum's submission to the ACCC on the Review of Transmission and Distribution Network Pricing. However, SCL would like to draw to the ACCC's attention a number of imperatives, which are of particular significance to the corporation.

SCL submits that:

- NECA's approach to the treatment of sunk cost is based on sound economic principles which least distort the market whilst continuing to provide the appropriate locational signals.
- As a general rule, network service providers should seek a market based commercial solution and regulatory intervention should only be considered as a last resort solution. The proposed net benefits test and market failure test for obtaining regulated network status must be clear and transparent in order to minimise the uncertainty of regulatory risk.
- Whilst the shift from a cost allocation focus is a positive move, there is an issue with the definition of beneficiaries. The definition of beneficiaries is critical, particularly in the case where an embedded energy project brings benefits to users of the network (generators and end use customers) in terms of improved system reliability and security, as well as reducing requirements for future capital expenditure. In this case end use customers also gain benefit from reduced loss factors.
- There is a robust economic rationale for the pass through of full reductions in TUOS charges to the relevant embedded generator.
- Generators should have the right to by pass existing networks, as this will introduce competitive market disciplines to network service providers, thereby facilitating the maintenance of a healthy and dynamic network infrastructure industry.

The following sub-sections expand on the above issues.

Treatment of sunk costs

The approach adopted by NECA is based on sound economic principles and thus there is no compelling argument to revisit this issue which has been the focus of considerable attention. SCL believes that NECA's approach for sunk costs to be borne by network customers is appropriate for the following reasons:

- Promotes economic efficiency, which is a central principle of the National Electricity Code. NECA's approach is the only robust and sensible way to address the treatment of sunk costs as it ensures the most efficient utilisation of the network. In addition, the cost recovery of residual sunk and fixed network charges directly from customers, least distorts the market in terms of decisions concerning generation dispatch, network use and location of investment.
- Provides appropriate locational signals. Locational signals are already provided to generators through marginal losses and the risk of capacity constraints. NECA's approach aligns the roles and responsibilities by allocating the costs to parties best able to manage the demand and the network infrastructure. This provides incentives

for network service providers to achieve optimal utilisation of the existing network as well as encouraging the use of demand side management.

Treatment of new investment

Under the current framework, investments by network service providers receive regulated status by default. SCL believes that as a general rule, network service providers should seek a market based commercial solution with regulatory intervention only being considered as a last resort. Network service providers should only be able to obtain regulated status for new investments, where these proposed new investments are able to satisfy both the net benefit test and a market failure test.

In these cases network service providers should bear the burden of proof to the ACCC by demonstrating a substantial threat to security and or reliability in the absence of the proposed network investment. The framework for determining eligibility for regulated status should be clear and transparent in order to minimise uncertainty and the associated regulatory risk, both of which may deter new investment.

Shift from a cost allocation focus and definition of beneficiaries

The past transmission and distribution pricing reviews recognised the benefits associated with embedded energy projects but there is in this case an issue with the definition of beneficiaries. This is illustrated by the following:

“All the beneficiaries of new investment in the transmission and, where there are shared benefits, the distribution networks should contribute to the costs of that investment in proportion to the estimated share of the benefits they derive from it. The aim should be, if at all possible, to introduce this cost sharing arrangement for all new investment projects, including new investment projects already included in Network Service Providers’ capital programs, on which work commences after 1 July 2000.”¹

Definition of beneficiaries is critical, because along with network investment, embedded energy projects could potentially benefit all users of the network (generators and end use customers) in terms of:

- enhancements in network reliability;
- system security;
- reduction in capacity constraints and associated capital expenditure to supplement existing systems.

It is also worth noting that end use customers also benefit from a reduction in loss factors associated with an increase in local generation capacity.

There is considerable international evidence that a narrow cost allocation approach severely disadvantages and adversely impacts upon the commercial viability of embedded energy projects.²

It is therefore important that the full contribution of embedded energy be recognised and reflected in network charges.

¹ NECA Transmission and Distribution Pricing Review (Final Report) Volume II – Consultants’ reports on the allocation of network investment costs and the cost reflective network pricing algorithm: role and refinements, July 1999, Page 17.

² Organisation for Economic Co-operation and Development, Penetration of Renewable Energy in the Electricity Sector (Annex 1 Expert Group on the United Nations Framework Convention on Climate Change Working Paper No. 15), August 1998.

Pass through of TUOS charges to embedded generators

SCL supports past transmission and distribution review findings that the full reductions in TUOS charges to a distribution network service provider as a result of an embedded generator locating in their area should be passed through to the embedded generator.

This will:

- Ensure that network charges for embedded generators are cost reflective in recognition of an embedded generator locating in a distribution network.
- Provide appropriate locational signals to embedded generators.
- Place embedded generators in the same competitive position as conventional generators.

Unrestricted right to by-pass existing networks

SCL supports the unrestricted right of market participants to by-pass existing networks for the following reasons:

- This contestability would provide competitive pressure on the network service provider to deliver an acceptable level of service quality and cost reflective network prices. These productivity and efficiency gains will flow through to end user customers.
- The unrestricted right to by-pass facilitates the establishment and maintenance of a dynamic and vibrant network service industry. This is achieved by providing the opportunity for new entrants to, enter the market with innovative solutions, take advantage of advances in technology and provide new sources of capital to fund essential infrastructure. This creates a climate conducive for the development of a culture of continuous improvement in efficiency and customer service, which is to the long-term benefit of customers within the electricity market.
- Competition is preferable to regulation and avoids the risk of entrenching or artificially prolonging the conditions that create a natural monopoly.

Conclusion

Appropriate network charges are critical to SCL's ability to provide competitive generation options to the market. **SCL is therefore committed to working closely with the ACCC, NECA and other regulatory bodies in the development of a commercially sound and equitable framework for transmission and distribution network pricing in the National Electricity Market.**