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File No: REG192-4
Our Ref: 08/886

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Dear Leigh

DRAFT NETWORK TARIFF STRATEGY

Thank you for the opportunity to comment on the Draft Network Tariff Strategy prepared as required by the Regulator's *Guideline for Approval of Network tariffs in accordance with the 2007 Determination November 2007*.

As set out in the Guideline, Aurora is required to publish and consult on a draft Network Tariff Strategy, and prepare a final Network Tariff Strategy by 30 April 2008. For each year from 1 July 2008, Aurora must prepare a Network Tariff Pricing Proposal that, amongst other matters, explains whether proposed amendments to Network Tariffs are consistent with the Network Tariff Strategy. The intention of the Network Tariff Strategy is to provide customers with information on the reasons for prospective changes in tariffs, to the extent that is possible. The Regulator does not approve the Network Tariff Strategy. The Regulator is required to approve the annual Network Pricing Proposal and must do so if the proposal complies with the 2007 Determination.

As you are aware, the requirements of the Determination in regard to the structure of tariffs is very broad and Aurora has considerable discretion in the design of network tariffs. However, the Regulator must, under the *Electricity Supply Industry (Tariff Customers) Regulations 1998*, approve changes in the terms and conditions of the retail tariffs paid by non-contestable tariff customers and which are available to contestable customers for the 12 month 'grace period' after contestability. In approving the retail tariffs charged by Aurora Energy Pty Ltd, the Regulator would have regard to the underlying components, including the structure of the network tariffs.

This response to the Draft Network Tariff Strategy is not intended to be a comprehensive response. It should not be taken to be an endorsement or otherwise of the Strategy, but is intended to draw attention to some aspects which do not appear to be consistent with the principles developed by Aurora and where the outcomes may not be efficient. As explained, Aurora has considerable discretion in drawing up its tariffs and it would not be appropriate for the Regulator, having given Aurora that discretion, to dictate outcomes. However, it is proper for the Regulator to question whether the outcomes are appropriate, in terms of promoting 'efficiency in the industry', and whether the Aurora material adequately meets requirements for transparency.

It is acknowledged that there is no single correct set of tariffs. Tariff design involves balancing a number of objectives, some of which may be in conflict with others. It should be recognised that any change from the current balance of tariffs will involve change in consumer behaviour and may impose costs, both to Aurora in the revised administration and to the customer in changing forms and pattern of use. There must be an offsetting and superior benefit to the community as a whole in greater efficiency, that is, lower cost to meet customer needs, to justify the change. It is important that Aurora clearly describe the problem and the objective, for example, to reduce demand in peak periods or to encourage use in periods when there is spare capacity in the system. It should follow that changing prices will change behaviour and this should be described, together with a description of the expected change in customer behaviour and the resultant benefits. While it is not always possible to quantify the cost and benefits, following the chain of cause and effect demonstrates the purpose and expected outcomes in a way that consumers can respond with an informed judgement about the merits of the proposal.

In Section 4.5.4, Aurora outlines its proposal for a Specified Demand Regime. Under this proposal, customers taking supply under a demand tariff would pay a lower rate for the demand element of the tariff up to a specified threshold, but would trigger much higher payments, possibly for an extended period, if the threshold is breached. This is a very significant change in tariff policy and Aurora proposes that the 'Specified Demand' tariffs will ultimately replace the Demand Tariffs. It would be beneficial if Aurora describes the purpose of this proposal, the effect on customers, the expected change in customer behaviour, which groups of customers may be adversely affected, and how Aurora or customers may manage any adverse effect.

Aurora proposes to introduce a seasonal component in a modified LV Time of Use tariff. At Section 4.5.7, it suggests that larger irrigators will find this tariff more attractive than the existing day / night tariff due to its seasonal component. In designing the seasonal rates, Aurora should consider whether the load characteristics of irrigation users (with high Summer demand) are sufficiently similar to the load characteristics of other demand tariff customers (generally with higher Winter demand) to justify a single tariff incorporating seasonal rates.

The customer impact analysis included in the paper shows that the network component (Tariff NO2) for the general business (Tariff 22) customers would increase by some 4 to 5 per cent per annum. Section 8.2.10 shows that, in general, the network component of LV demand tariffs would see increases of the order of 10 per cent per annum. The effect would be an increase in charges under the LV demand tariff by more than 20 per cent relative to the general commercial tariff, over the four year period. The effect of this would be to raise the load factor at which customers would choose to take supply under a demand tariff rather than under the general tariff, such that fewer customers would have an incentive to stay on a

demand tariff. The effect of this is that fewer customers would be exposed to signals to moderate demand. This would seem to be contrary to the intention to expose a larger number of customers to cost-reflective price signals. This warrants further explanation. Further, there are significant increases in costs for LV customers compared with HV customers after period 2. The paper does not explain the reasons for such significant differences in the proposed tariffs.

The pricing principles require, amongst other matters, that the tariffs be determined having regard to 'the observed proportion of fixed and variable charges applied in other NEM jurisdictions for a similar service.'. Although Aurora claims to have taken this into account, the paper does not present any evidence to support the claim.

I also note that the scheme for tariff approval adopted in the *Guideline* is based on the parallel provision of the *National Electricity Rules* which would apply to Aurora if the Determination had been made under the *National Electricity Rules* rather than under the *Tasmanian Electricity Supply Industry (Price Control) Regulations 2003*. The *Rules* impose side constraints such that the average rate of change for a tariff class is restricted by reference to the average rate of change generally, or by CPI. There is no such restriction in the 2007 Determination. Nevertheless, Aurora should I believe have regard to the adverse impact of significant and sudden change for particular sectors on top of the significant average increase arising from the 2007 Determination.

Finally, Aurora frequently uses the terms 'large customer' and 'small customer' without defining the terms, and the times are not specified as Eastern Standard Time or otherwise.

I thank you for the opportunity to comment and look forward to the further development of the Network Tariff Strategy taking account of this and other responses.

Yours sincerely

Andrew Reeves
REGULATOR

12 March 2008