Electricity Network Regulation
Productivity Commission
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23 November 2012

Dear Secretariat

Submission to Electricity Network Regulatory Frameworks Draft Report

GDF SUEZ Energy Australia welcomes the opportunity to comment on the Productivity Commission's draft report on electricity network regulatory frameworks.

GDF SUEZ Energy Australia (GDFSEA), formerly International Power-GDF SUEZ Australia, is wholly owned by GDF SUEZ S.A. and a business line of GDF SUEZ Energy International.

GDF SUEZ Energy International is responsible for GDF SUEZ's energy activities in 30 countries across six regions worldwide (Latin America, North America, UK-Europe, the Middle East, Turkey and Africa, Asia and Australia). Together with power generation, the company is also active in closely linked businesses including downstream LNG, gas distribution, desalination and retail. GDF SUEZ Energy International has a strong presence in its markets with 77 GW gross capacity in operation and a significant program of 10 GW gross capacity of projects under construction as at 30 June 2012. The business has more than 11,000 employees and generated revenues of €16.5 billion in 2011.

In Australia, the company owns and operates 3,500MW (gross) of renewable, gas-fired and brown coal-fired plants in Victoria, South Australia and Western Australia. Its retail business, Simply Energy, has more than 300,000 electricity and gas accounts in Victoria and South Australia.

General comments

GDFSEA notes the considerable effort undertaken by the Productivity Commission in preparing the Electricity Network Regulatory Frameworks Draft Report (draft report), and agrees with many of the conclusions, including that inefficiencies in the regulatory environment have contributed substantially to recent electricity price increases.

GDFSEA supports many of the recommendations in the draft report, and believe that if implemented, they would improve the network regulatory environment. There are however, some recommendations that GDFSEA does not support, and rather than comment extensively on those that are supported, we have instead outlined the areas of disagreement in the following sections.

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Demand management

GDFSEA does not support the draft report chapter 10 recommendation in relation to demand management technologies. GDFSEA supports the rollout of smart meters but believes that a market driven rollout of smart meters is preferable to a mandated roll out by distributors. As has been demonstrated by the Energy Retailers Association of Australia, retail competition creates incentives for retailers to install and deliver the smart meter services that customers seek in a cost-effective manner. As a result, customers receive better outcomes than can be achieved under a government mandated distributor led roll out, including lower costs, better services and more innovative retail products. We note that the Australian Energy Markets Commission (AEMC) has also favoured market-driven delivery of smart metering services to customers in their recent Power of Choice review.

Facilitating a market-driven rollout of smart metering will require changes at both a government and distributor level. Jurisdictional governments will need to remove artificial barriers that currently prevent retailers from providing small customers with competitive metering services. To address this regulatory failure, all remaining exclusivity provisions (including those in Victoria) that provide distributors with a monopoly over the delivery of metering services must end.

Metering charges will also need to be unbundled from network charges. The bundling of metering charges with network charges acts as a significant barrier to retailers rolling out smart metering services. If a retailer did replace a householder's manually-read meter with a smart meter, the retailer would still need to pay the bundled network charge, making the business case for replacement uneconomic.

Further, exit fees charged by distributors for displaced meters should be aligned with the early termination fee principles established by the National Energy Consumer Framework, so that the fee charged is no more than a reasonable estimate of costs resulting from early termination (the depreciated value of the remaining life of the asset).

Regarding the proposed complementary reforms to support demand management (chapter 12 of the draft report), GDFSEA supports the participation of demand in the market, as was envisaged when the NEM was designed. GDFSEA does not however, support the introduction of specific mechanisms which favour certain business models to promote demand side participation. Such approaches are distortionary, and interfere with wholesale price signals, penalising existing market participants and discouraging new entrants.

This is most evident at the margin of peak demand, where peaking capacity on the supply side, and demand responses, are providing approximately equivalent services (demand response may be a lesser form of capacity because its dispatch is less certain); however facilitated demand response would be receiving additional revenue, equivalent to a capacity payment, as well as avoiding the economic cost of electricity delivered.

Time-based pricing

GDFSEA supports the principle of cost reflective pricing for networks and welcomes the efforts of the Productivity Commission to apply this principle to customer charges. Cost reflective prices are essential if customers are to be motivated to consider the impact of their electricity usage on future network costs in the same way that they are increasingly considering the energy component of their costs.

GDFSEA believe that time-based energy pricing provides a poor surrogate for cost reflective pricing for networks. As recognised by the Productivity Commission, network costs are fixed based on the maximum demand that the system experiences on a few days of the year, but are recovered via a variable energy charge. This results in distorted price signals to consumers that lead to inappropriate and economically inefficient consumer behaviours. In addition, cross subsidies between customers are created as high peak demand / low energy usage customers are subsidised by lower peak demand customers with high energy usage[1].

GDFSEA also notes that the success of smart metering technologies and the introduction of cost-reflective pricing is dependent upon customer acceptance of these new approaches to electricity pricing. As demonstrated by Victoria's smart meter rollout, if customers are not brought along on the journey then there can be significant push back from the very constituents that the changes are predominantly meant to benefit.

Assisting customers to understand the logic of time of use pricing is the key reason why GDFSEA favours a market-driven rollout of smart metering technologies. Rather than technologies and different pricing structures being forced upon them, customers will instead be sold the benefits that the different arrangements can deliver to them. Again, GDFSEA strongly urges the Productivity Commission to review the smart metering papers that were released by the Energy Retailers' Association earlier this year.

It is also noted that the Productivity Commission's recommendations in relation to time-based pricing seem to be predicated on a distributor-led rollout of smart meters, which would require amendment if a rollout is undertaken by the competitive retail market. The recommendations also appear to pre-suppose that the necessary precursors for time-based pricing already exist in the market. For example, recommendation 11.1 of the draft report suggests that the SCER have oversight the implementation of time-based pricing. This seems premature given that accumulation metering remains the most common form of metering in the NEM. The Productivity Commission may wish to consider qualifying its recommendations in relation to time-based pricing, to signal that much work needs to be done across the NEM before the industry is in a position to move toward this approach.

Benchmarking

GDFSEA has some concerns regarding the heavy resource burden that the draft report (chapter 8) recommendations would impose on the Australian Energy Regulator (AER), and whether this represents an efficient approach. We agree that there is a need for greater transparency on the specific details within AER regulatory decisions for networks. For example, GDFSEA believes that there should be greater transparency on how networks actually spend the money that the AER allows them through their regulatory price path. Greater transparency would provide the opportunity for stakeholders to understand the basis for each decision, and compare it with other decisions.

Benchmarking of network businesses faces the challenge that many of the network businesses are quite distinct from each other on a number of measures. The Productivity Commission has recognised this and proposed a range of approaches to benchmarking designed to account for these differences. However, the implementation and ongoing management of the proposed benchmarking would represent a substantial task for the AER and network businesses, and would therefore impose an additional cost on the industry, and therefore ultimately, customers.

[1] For a more detailed explanation, see International Power GDF Suez submission to AEMC Power of Choice Issues Paper dated 26 August 2011, on web at http://www.aemc.gov.au/Media/docs/International%20Pwer-e8169c91-0736-46ef-aa94-130ca180ef3f-0.PDF

The objective of improving assessment metrics for regulated network businesses is supported. However, the proposed suite of benchmarking proposals would be complex, costly and of doubtful effectiveness. For example, using benchmarking to compare Energex, Ausgrid and CitiPower would seem to be a fruitless task because the networks are so different, face different geographies that significantly impact per-customer unit costs, different customer demands and have experienced much different histories that have determined where they are today.

We therefore suggest that as a first step, greater transparency on distributors' activities, including actual spend against what they forecast, and how that money has been spent, would be a good starting point for improving the effectiveness of the regulatory process. Following this, the value of further targeted benchmarking could be re-assessed.

Governance

GDFSEA notes that the AER relationship with electricity industry participants is somewhat different to the traditional role of the ACCC. The AER has on ongoing relationship with the electricity industry, unlike the ACCC which generally has a more adversarial role invoked when a competition issue is detected. This does not necessarily mean that the AER should be separated from the ACCC. However in structuring and resourcing the AER, it should be recognised that there needs to be an adequate level of dedicated resources to deal with the ongoing complexity of the electricity market regulatory environment.

GDFSEA strongly opposes the recommendation to provide the South Australian Minister a broader power to make electricity market Rules. The existing Rule change process provides an appropriate mechanism for all stakeholders to initiate, and participate in Rule changes. Of greater concern to industry participants is regulatory risk due to unexpected changes. Increasing the power for the government to bypass the Rule making process increases regulatory risk, adding further uncertainty for industry participants which will ultimately be reflected as additional costs to consumers.

Customer Benefits

GDFSEA agrees with the Productivity Commission observation that the overarching objective of the regulatory regime is to advance the long-term interests of electricity customers. One caution that should be observed in any move to reinforce consideration of customer interests is the need to avoid focusing on short term gains which are likely in the long run, to contribute to a customer detriment. This is important, as the temptation for customer groups and political interests to focus on short-term gains is ever present; however real customer interests are best served by taking a long-term view.

Nowhere is this more evident than in regulatory certainty for generation investments. Short-term gains for consumers, such as those sought in the South Australian regulator's recent draft decision on the wholesale cost contribution to regulated tariffs, may be achieved at the expense of investor confidence that will either be expressed in disinterest in building new capacity, or higher risk premiums in the prices for new entrant capacity.

Reliability

GDFSEA is generally supportive of an approach to setting reliability standards which take account of customer's assessment of their own needs. From a practical perspective, such an approach will need to take account of the fact that network reliability settings typically encompass wide geographic areas which will include a range of customers with perhaps inconsistent reliability needs. In the end, some level of pragmatism will be necessary to avoid over-analysis leading to costly outcomes with little additional benefit.

Government Ownership

GDFSEA supports the Productivity Commission recommendations for governments to move away from state ownership of electricity assets. Where governments retain ownership, they are held accountable by the public for electricity cost and service level outcomes. This leads to governments taking decisions with a short-term perspective, seeking to provide immediate redress to public concerns, rather than seeking the best outcome in the long term. This can be de-stabilising for the electricity industry and increases the regulatory risk to participants, which ultimately is not in the customer's long-term interests.

Further, we remain convinced that the commercial disciplines driven by the values of private owners ultimately result in lower costs for consumers.

Interconnectors

GDFSEA notes the Productivity Commission comments that there is no evidence of insufficient interconnector capacity. One of the reasons that interconnectors are currently underutilised is the inability for generators to enter into firm hedging contracts across regional boundaries. As a result, generators find it difficult to effectively manage their exposure to inter regional prices, and therefore are reluctant to rely on interconnectors. If more effective inter-regional hedging was available, it is likely that interconnector utilisation would increase. We therefore are pleased that the Productivity Commission has endorsed the Transmission Frameworks Review which is seeking to improve generator firm access rights and inter regional access.

GDFSEA trusts that these brief comments are helpful to the Productivity Commission in its deliberations on the important matters raised in the draft report.

Yours sincerely

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