



# **CitiPower, Powercor, United Energy**

## **Revised Cost Allocation Methods**

**AER Final Decision**

October 2020

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AER Reference: 64082

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## Shortened forms

### Table text heading

AER	Australian Energy Regulator
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CAM	Cost Allocation Method
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Distributor, DNSP	Distribution Network Service Provider
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guidelines	Distribution Cost Allocation Guidelines
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NEL	National Electricity Law
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NEM	National Electricity Market
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Rules, NER	National Electricity Market Rules
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# 1 Introduction

## 1.1 Summary

On 25 August 2020 CitiPower, Powercor and United Energy submitted to the AER, for approval, revised Cost Allocation Methods (CAMs) for their Victorian electricity distribution systems — see Appendix A to this paper.<sup>1</sup>

CitiPower, Powercor and United Energy provide electricity distribution services across large parts of Melbourne and all of regional western Victoria.

A CAM is used to separately account for the costs of providing electricity distribution services, including from other services the distributor might provide. CitiPower, Powercor and United Energy proposed their revised CAMs take effect from 1 July 2021.<sup>2</sup> This means the revised CAMs are also applicable to the distribution determinations which we are currently undertaking with the Victorian distributors for the 2021-26 regulatory control period.

We have determined the CitiPower, Powercor and United Energy proposed CAMs:

- accord with the requirements of the National Electricity Law (NEL) and National Electricity Rules (the rules)
- give effect to and are consistent with our Distribution Cost Allocation Guidelines (distribution guidelines).

Accordingly, we have approved the CitiPower, Powercor and United Energy proposed CAM revisions under clause 6.15.4(c) of the rules.

## 1.2 Background

The AER is responsible for regulating revenues of the electricity distribution businesses in Victoria in accordance with the NEL and the rules. Chapter 6 of the rules provides further details on the economic regulation of electricity distribution services in Victoria.

Cost allocation concerns attributing a regulated business' costs, or allocating shared costs, between distribution service categories and non-regulated business sections. The different services provided by distributors are defined in the NEL and the rules. They are:

- direct control services, comprising:
  - standard control services
  - alternative control services
- negotiated distribution services
- unclassified, or unregulated, services.

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<sup>1</sup> CitiPower, *Cost Allocation Method*, August 2020; Powercor, *Cost Allocation Method*, August 2020; United Energy, *Cost Allocation Method*, August 2020.

<sup>2</sup> CitiPower, *Cost Allocation Method*, August 2020, p.3; Powercor, *Cost Allocation Method*, August 2020, p.3; United Energy, *Cost Allocation Method*, August 2020, p.3..

A further category of services is identifiable: non–distribution services. We do not, nor are we able to, regulate these services.

In our distribution determinations we classify distributor services to the above categories based on factors specified by the rules. The prices distributors charge for the different categories of distribution services depend on the costs incurred in providing those services. It is therefore important that cost allocation between service classifications accurately and fairly represents costs incurred in providing those services. We rely upon historical and forecast costs allocated in accordance with an approved CAM to determine prices charged, or revenues raised, by distributors such as CitiPower, Powercor and United Energy.

Distribution regulatory proposals, or the regulatory arrangements proposed by distributors to us for a particular regulatory control period, must comply with an approved CAM. The revised CAMs subject to this decision paper will be used by CitiPower, Powercor and United Energy to develop their future distribution regulatory proposals including their revised proposals for the 2021-26 regulatory control period. The distributors will also use their revised CAMs to report to us annually.

Following our approval, the revised CAMs will remain relevant to the distributors' reporting and regulatory proposals until we approve further CAM variations.

## 2 Rule requirements and assessment

### 2.1 The rule requirements

For DNSPs:

- Clause 6.15.4(a) of the rules requires a DNSP to submit to us for approval a document setting out its proposed CAM.
- Clause 6.15.4(b) requires that a CAM give effect to and be consistent with our distribution guidelines.
- Clause 6.15.4(c) provides for us to approve or refuse to approve a CAM submitted under paragraph (a).
- Clause 6.15.4(f) provides for a DNSP to amend its CAM from time to time, subject to our approval.

### 2.2 Assessment process

CitiPower, Powercor and United Energy initially submitted revised CAMs on 31 January 2020 within the packages of materials for their distribution determination proposals for the 2021-26 regulatory control period. The three distributors indicated within their distribution determination proposals that they had been prepared in accordance with the proposed revised CAMs, not in accordance with the approved CAMs for each of the three distributors.

The approach taken by CitiPower, Powercor and United Energy is inconsistent with the rules' requirements. For example, rule 6.5.6(b)(2) requires the operating cost forecast within a building block proposal to be in accordance with an approved CAM.

Provision of the CAM amendments to the AER within a large package of materials without giving prior indication or notice of the amendments is inconsistent with the requirements of our Cost Allocation Guideline.<sup>3</sup> Clause 4.2(a)(1) of our Cost Allocation Guideline states that a distributor can only amend its CAM if it applies in writing to the AER to make such an amendment.

We advised CitiPower, Powercor and United Energy that the three regulatory proposals were not provided in accordance with the rules and that we had not received appropriate written applications to vary the existing approved CAMs.

While the three distribution regulatory proposals were not prepared in accordance with approved CAMs as required by the rules, we considered they were sufficiently compliant to proceed with our assessment. Our approach is consistent with rule 6.9.3(6) which requires the AER to conclude that regulatory proposals are compliant, or are sufficiently compliant, with the NEL and NER before proceeding with our assessment.

Alongside our assessment of the three regulatory proposals we undertook to assess the three proposed CAM revisions. However, to achieve compliance with clause 4.2(a)(1) of our Cost Allocation Guidelines we asked CitiPower, Powercor and United Energy to resubmit the

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<sup>3</sup> AER, *Cost Allocation Guidelines for Victorian Electricity Distribution Network Services Providers*, June 2008.

proposed CAM revisions with an appropriate covering letter seeking AER approval. That was provided by CitiPower, Powercor and United Energy on 31 March 2020.

Our subsequent assessment of the three proposed CAM variations found a small number of issues meant that the new CAMs could not be approved. We advised CitiPower, Powercor and United Energy of the issues we identified. As a result of that communication the distributors formally withdrew the three CAM variations, undertook to address the issues identified and to re-submit the CAM revisions.

On 25 August 2020 CitiPower, Powercor and United Energy re-submitted CAM revisions to us for approval. It is these iterations that are the subject of our approval.

## 2.3 CAM revisions

CitiPower, Powercor and United Energy sought AER approval of the attached revised CAMs under clause 6.15.4(f) of the rules. The CAMs provide details on corporate structure, attribution of direct costs, allocation of indirect costs, cost recording and record keeping systems.

CitiPower, Powercor and United Energy submitted that the drivers for amending their CAMs are:<sup>4</sup>

- corporate structure changes
- operational structure changes
- updated service classifications for the 2021-26 regulatory control period.

The issues we identified with the initial iterations of the proposed CAM revisions related to:

- allocation of some corporate costs to unregulated services
- alignment of United Energy's allocation of meter data costs to the proposed CitiPower and Powercor CAMs
- allocation of metering communications costs between standard control and alternative control services.

The 25 August 2020 iterations of the three CAM revisions address the above issues.

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<sup>4</sup> CitiPower, Powercor, United Energy, letter to AER: *Amending our Cost Allocation Methods*, March 2020.



### 3 Consistency with our Distribution Cost Allocation Guidelines

This section sets out our assessment of the CitiPower, Powercor and United Energy proposed CAM revisions against the requirements of our Cost Allocation Guidelines. We consider the three proposed CAM revisions are compliant.

#### 3.1 CAM assessment

The format and content of a CAM are regulated by clause 3.2(a) of our guidelines. Table 1 compares the proposed CAMs against the requirements of clause 3.2(a). The proposed CAMs for CitiPower, Powercor and United Energy are almost identical so page number references in Table 1 are consistent across the three proposed CAMs.

**Table 1 CAM assessment**

Clause 3.2(a) of the AER’s Distribution Cost Allocation Guidelines	CAM references
(1)-(2) A version history and date of issue for the document	Compliant. See page 1.
(3) A statement of the nature, scope and purpose of the document and the way in which it is to be used by the distributor.	Compliant. See page 4
(3) Details of the accountabilities within the distributor for the document in order to set out clearly:  A. the distributor’s commitment to implementing the CAM; and  B. responsibilities within the distributor for updating, maintaining and applying the CAM and for internally monitoring and reporting on its application.	Compliant. See page 5.
(4) A description of the distributor’s corporate and operational structure to enable the AER to understand how the distributor is organised to provide its distribution services.	Compliant. See pages 6 and 7.
(5) A specification of the categories of distribution services that the distributor provides to which costs are to be attributed or allocated and the types of persons to whom those services are provided.	Compliant. See pages 8 and 9.
(6) The distributor’s detailed principles and policies to be used for attributing costs directly to, or allocating costs between, categories of distribution services that meet the requirements of clause 2.2 of the Guidelines. For the avoidance of doubt, this includes the attribution or allocation of costs relating to any related party transactions.	Compliant. See pages 10 to 15.
(7) A description of how the distributor will maintain records of the attribution or allocation of costs to, or between, categories of distribution services to enable any such attribution or allocation to be:	Compliant. See page 5.

A. demonstrated to the AER, in accordance with clause 5.2 of these Guidelines; and

B. audited or otherwise verified by a third party, including the AER, as required.

(8) A description of how the distributor will monitor its compliance with the CAM and the Guidelines.	Compliant. See page 5.
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(9) Details of the proposed date on which the CAM will commence, having regard for clause 4.1(d) of these Guidelines.	Compliant. See page 3.
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