

20 February 2013

Mr Warwick Anderson  
General Manager  
Network Regulation Branch  
Australian Energy Regulator  
PO Box 3131  
Canberra ACT 2601

Dear Mr Anderson

### **Formulae for control mechanisms**

ActewAGL Distribution welcomes the opportunity to comment on the AER's *Formulae for control mechanisms – discussion paper* released on 15 February. As recognised in the discussion paper, the November 2012 amendments to the *National Electricity Rules* include a new requirement that the AER include control mechanism formulae in its *framework and approach paper*. Given that the formulae form an important part of the control mechanism and their lack of exposure in the process to date, it is appropriate for the AER to consult on them before releasing the framework and approach paper by 28 March 2013.

ActewAGL Distribution notes that the new rules also include requirements for the AER to include in the framework and approach paper an explanation of “the manner in which any true-up between the placeholder and full determination will be carried out for DNSPs that are subject to a price cap form of regulation” and “the manner in which any true-up will be carried out for the DNSPs providing alternative control services that are capable of being trued-up”.<sup>1</sup> While we accept that these matters are not within the intended scope of the current discussion paper ActewAGL Distribution considers that consultation on them is appropriate.

Comments on the proposed formulae for standard control and alternative control services in the ACT are set out in separate sections below.

### **Formulae for the control mechanism for standard control services in the ACT**

ActewAGL Distribution supports the AER's proposal in the discussion paper to apply an average revenue cap to standard control services in the ACT, and notes that this represents the outcome of extensive consultation on this matter. We note below some differences in detail between the control mechanism proposed and that currently applied.

In the current control mechanism, the most recent calendar year's actual data (denoted ct-1) are used when setting the maximum allowed average revenue (MAAR) cap and checking compliance. These data are verifiable, as required under the 2009 Final Decision. The proposed formulae instead specify use of less recent financial year data (denoted t-2). ActewAGL Distribution seeks to confirm the AER's specification of financial year data rather

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<sup>1</sup> AEMC 2012, *Rule Determination: National Electricity Amendment (Economic Regulation of Network Service Providers) Rule 2012 and National Gas Amendment (Price and Revenue Regulation of Gas Services) Rule 2012*, November, p. 247

than the most recent calendar year's verifiable actual data.

The AER also proposes to use t-2 quantities to determine the average values for the "adjustments" in the MAAR formula. This represents a shift away from the current approach where the forecast quantities are used to calculate the annual adjustments. The most appropriate denominator is throughput in the pricing year and quantities in the t-2 year may be a poorer approximation of those quantities than the forecast in the final determination.

The AER should also note that, on page 15 of the discussion paper, the word "average" has been omitted from the definition of  $AAR_t$ , while on page 14 the subscript on CPI has been omitted.

### **Formulae for the control mechanism for alternative control services in the ACT**

ActewAGL Distribution remains concerned about the AER's proposed approach to the control mechanism for alternative control services and seeks further consultation with the AER on this matter before the framework and approach paper is finalised. The AER's preliminary position in June 2012 was to apply price cap regulation to services classified as alternative control services for the 2014-19 regulatory period. Our August 2012 response to the preliminary positions paper put forward a preferred model which effectively involved applying a price cap to a *basket* of metering services, rather than to each individual service. ActewAGL Distribution considers that this approach provides flexibility to adjust relative prices during the period, to respond to changing relative costs or demand conditions, without the need for detailed assessments for each service. In the current discussion paper, the AER retains its preliminary position of applying a price cap to each individual alternative control service without consulting on ActewAGL Distribution's proposed mechanism.

ActewAGL Distribution has proposed an alternative mechanism to the AER's schedule of price caps. The proposed mechanism can be expressed as follows:

- Prices in each year must be set so that the total revenue that would be collected on a fixed basket of services is less than the maximum allowable revenue
- The cap will be escalated each year by CPI inflation and the X-factor
- The cap in year one will be set in the final decision
- The basket of services should represent the appropriate average relative consumption levels of the services, and would also be fixed at the time of the final decision

and represented as a formula as follows:

$$MAR_t \geq \sum_{i=1}^n \sum_{j=1}^m p_{ij}^t \bar{q}_{ij}$$

$$MAR_t = MAR_{t-1}(1 + CPI_t)(1 - X_t)$$

where

$MAR_1$  is the notional revenue collected from the basket, to be determined in the final decision

$p_{ij}^t$  is the price of component i on tariff j in year t

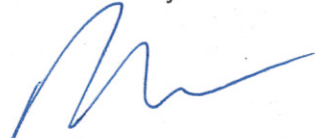
$\bar{q}_{ij}$  is the notional basket of services used to set prices

$CPI_t$  is the percentage increase in the consumer price index in year t, to be decided in the final decision

$X_t$  is the X-factor in year t, to be decided in the final decision

Please contact Chris Bell, Manager Regulatory Affairs, on 6248 3180 if you would like to discuss our submission.

Yours sincerely



David Graham  
Director Regulatory Affairs and Pricing