17 May 2013

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Dear Chris

Submission on Shared Assets Guideline Issues Paper

This letter is the Energy Users' Association of Australia response to the AER's Shared Assets Guideline Issues Paper. We thank the AER for the opportunity to provide our views on this Issues Paper.

In general we agree with the broad direction of the AER's approach, although we suggest a stronger focus on the interests of users in the income derived from shared assets. Our responses to the AER's questions follow:

Response to Question 1

We suggest that the AER's proposed materiality of 1% of revenues is too low. For example 1% of Energex's 2015 regulated revenue will be $18m. This is likely to translate (in view of rising regulated revenues) to more than $90m over a five year regulatory control. This is much too high a threshold before the guidelines should apply. Accordingly, if the AER is seeking to define a threshold as a percentage of regulated revenues, we suggest a threshold not higher than 0.25%.

Response to Question 2

We do not agree with the proposal that the AER will forecast and not subsequently true-up for actuals. There is no allocative or productive incentive detriment associated with such true-up (the true-up does not involve an ex-post efficiency assessment) and trueing-up at the end of the regulatory control period for actuals ought to be administratively straight-forward. Its not immediately clear to us that a true-up is contrary to the National Electricity/Gas Rules, but if

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it is, the AER should seek to changes these Rules, we can see no plausible benefit (and potentially considerable detriment) from the use of forecasts rather than actuals.

Response to Question 3

We don't agree. We are not convinced that the level of reporting should be de-linked from the threshold for application of the guidelines. Accordingly we suggest adequate reporting apply whenever the threshold for application of the guidelines applies.

Response to Question 4

Our response to this is dealt with in our response to the next questions.

Response to Question 5

Yes, perhaps. Our suggestion on the treatment of shared assets does not involve adjustment of costs separately to regulated revenues. So, yes, a method should be established in the guidelines but no it should not specify the treatment of costs (at least pursuant to our proposed approach)

Response to Questions 6, to 9

These questions all relate to similar aspects of the same issue and so are answered together.

We are not convinced that regulated network service providers should be provided with significant incentives to increase revenues from shared assets. We accept that users potentially benefit from unregulated shared asset income, but this benefits needs to be set against the prospect of effective subsidies from energy users to other unregulated users of infrastructure whose fully-absorbed cost users are bearing. In addition, and perhaps more importantly we would much rather that the managers of the network service providers were incentivised to focus their attention on the efficient development and operation of regulated assets, rather than to provide opportunities for these managers to profit by increasing income from unregulated benefits provided by assets that users have funded.

Accordingly some mild incentive may be useful (so that network service providers don't forego easy opportunities to extract value for the benefit of energy users). But this incentive should not be so strong as to distract their attention in way that deliver super-profits for their owners, at the expense of their focus on their core business.

Our proposal for an appropriate distribution of the income from shared assets is as follows:

1. Income from charges for the provision of unregulated services from shared assets and annual capital contributions from the users of such services should be recorded annually.
2. Incremental costs incurred by the network service provider in providing unregulated services from shared assets to unregulated users should be recorded annually. These incremental costs are the avoidable cash costs associated with the provision of unregulated services from shared assets. They must not include any recovery of depreciation, return, tax or operating expenditure that has been compensated through the regulated charges.
3. Users should receive 90% of the income in (1) less the incremental costs (in (2)) as an off-set in the regulated income. NSPs would therefore recover their incremental costs plus 10% of the unregulated income from shared assets.

Two examples illustrate this approach:

Example 1

A network service provider (NSP) has a fleet of heavy duty vehicles which are not used for much of the year. A specialist transport company offers to pay the NSP a lease fee of $10m per year to use the vehicles for 40 days per year. The NSP incurs additional maintenance and administration expenditure of $1m per year as a result of this lease. Under our proposed arrangement, the NSP should reduce regulated network service charges by $8m (90% of the $10m income plus the $1m costs) The NSP recovers its incremental costs (of $1m) and achieves additional fee income of $1m

Example 2

An NSP leases fibre-optic capacity on its state-wide transmission infrastructure for $40m per year to a telecom service provider. In configuring this capacity to be useful to the telecom service provider, the telecom service provider requires capital expenditure of $5m to be incurred by the transmission network service provider. The telecom service provider pays this capital contribution to the network service provider directly. In providing this unregulated service, the NSP also incurs $3m of on-going expenditure that it would otherwise not incur. Under our proposed arrangement, regulated charges in the first year (when the capital enhancement is done) should be reduced by $36m (90% of the $40m income) less $5m less $3m = $28m per year. In subsequent years the regulated charges should be reduced by $36m less $3m = $33m per year. In this way the NSP recovers all its incremental expenditure related to the provision of this service and in addition retains a margin on the additional shared asset income of $3m per year.

We would be pleased to discuss this further should the AER wish.

Yours sincerely,

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