

17 February 2012

Mr Chris Pattas
General Manager
Australian Energy Regulator
GPO Box 520
Melbourne VIC 3001

Dear Mr Pattas

**DRAFT CONNECTION CHARGE GUIDELINES FOR ELECTRICITY CUSTOMERS
UNDER CHAPTER 5A OF THE NATIONAL ELECTRICITY RULES**

Endeavour Energy is pleased to make this submission to the Australian Energy Regulator (AER) on its "*Draft connection charge guidelines for electricity retail customers, under Chapter 5A of the national Electricity Rules*" (the Draft Guidelines) and its accompanying Explanatory Statement.

Endeavour Energy notes that the purpose of the guideline is to set the method that must be followed by Electricity Distribution Service Providers in determining the capital contribution for new retail customers connecting to the distribution networks.

The Explanatory Statement provides the background and the AER's response to several issues and alternate options for calculating connection charges raised in previous consultations, and informs the development of the Draft Guidelines.

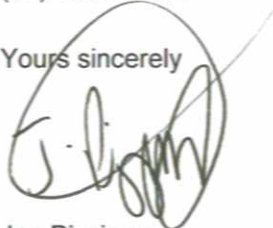
Attached is Endeavour Energy's detailed response to the Draft Guideline.

I note that the AER is also currently consulting on the Classification of Electricity Distribution Services in the ACT and NSW. It will be important to ensure consistency between the Draft Guidelines and the classification of services.

As discussed in the accompanying attachment, there are several connection charge issues requiring further analysis and consideration prior to finalisation of the Connection Charge Guidelines. Among these issues is the operation of the Accredited Service Provider Scheme in NSW.

If you would like to discuss any of these matters further, please contact Mr Erik Beerden, Regulatory Affairs Manager on telephone number (02) 9853 6904 or Mr. Michael Martinson, Manager Network Regulation on (02) 9853 4375.

Yours sincerely



Joe Pizzinga
Chief Financial Officer

Attachment 1

DRAFT CONNECTION CHARGE GUIDELINES FOR ELECTRICITY CUSTOMERS UNDER CHAPTER 5A OF THE NATIONAL ELECTRICITY RULES

Connection Charge Principles

Connection Charge Guidelines developed by the AER must, among other things, describe the circumstances under which a Distribution Network Service Provider (DNSP) may receive a capital contribution, and how the amount of any such contribution is to be determined¹.

The connection charge principles set limitations on capital contributions paid by retail customers towards the cost of an augmentation (insofar as it involves more than an extension). However, they would also appear to limit capital contributions paid by retail customers towards the cost of connection assets.

Clause 5A.E.1(b) states:

"A retail customer (other than a non-registered embedded generator or a real estate developer) who applies for a connection service for which an augmentation is required cannot be required to make a capital contribution towards the cost of the augmentation (insofar as it involves more than an extension) if:

(1) the application is for a basic connection service; or

(2) a relevant threshold set in the Distribution Network Service Provider's connection policy is not exceeded.

Note

In general, the intention is to exclude deep system augmentation charges for retail customers."

An augmentation is defined in the NEL as "of a transmission or distribution system means work to enlarge the system or to increase its capacity to transmit or distribute electricity".

A distribution system is defined under the National Electricity Rules (NER) as:

"A distribution network, together with the connection assets associated with the distribution network, which is connected to another transmission or distribution system.

Connection assets on their own do not constitute a distribution system."

Therefore, an augmentation includes *premises connection assets*. However, an augmentation does not include an *extension* unless 'outside the present boundary' of the DNSP network owned, controlled and operated by the DNSP².

Guidance as to what is 'outside the present boundary' of the DNSP network owned, controlled and operated by the DNSP is provided in a note to clause 6.7A.1(b)(2) and clause 5A.B.2(b)(5)(i) of the NER.

Under clause 6.7A.1(b) of the NER, any connection policy developed by a DNSP must be consistent with the connection charge principles and the connection charge guidelines. This includes specifying the categories of persons that may be required to pay a connection charge and aspects of the connection service. An example to clause 6.7A.1(b)(2) of the NER states:

¹ Cl. 5A.E.3(c)

² An 'extension' is defined in the National Electricity Rules

"Example

The Distribution Network Service Provider might (for example) make separate connection charges for the provision of a connection asset and for making a necessary extension to, or other augmentation of, the distribution network."

On this wording, a connection asset is not an extension. This distinction is reinforced in clause 5A.B.2(b)(5)(i) requiring the details of connection charges for the terms and conditions of the proposed model standing offer for basic connection services to include:

"the cost of any necessary *extension* to the *distribution system* for which provision has not already been made through existing *distribution use of system charges* or a tariff applicable to the *connection*".

The distinction between a connection asset and an extension is also consistent with the definitional meaning of an augmentation to enlarge the distribution system.

As the extension is to the distribution system and not the distribution network, clause 5A.E.1(b) would prevent a DNSP from charging a capital contribution for connection assets for a basic connection service.

Classification of Connection Services

Endeavour Energy notes that a separate consultation on the Classification of Electricity Distribution Services in the ACT and NSW is currently being conducted by the AER. In developing the connection charging guidelines, the classification of services should accommodate the circumstances in which connection services may be provided by persons other than DNSPs (and are therefore contestable)³.

NSW is the only jurisdiction which operates a contestability regime which allows Accredited Service Providers (ASPs) to provide connection services.

The Explanatory Statement includes the statement that "*the AER's connection charge guideline does not pre-empt or bind the AER to apply any particular service classification as part of a distribution determination.*"⁴

The classification of distribution services forms the basis of connection charging and underpins a distributor's connection policy to be approved by the AER⁵. The classification of services also informs the basis of a distributor's regulatory proposal made to the AER in respect of a Distribution Determination⁶.

Under clause 6.7A.1(b), a DNSP's connection policy must be consistent with the guidelines and must specify:

- (i) the categories of persons that may be required to pay a connection charge and the circumstances in which such a requirement may be imposed; and
- (ii) the aspects of a connection service for which a connection charge may be made; and

³ Cl. 5A.E.3(e)

⁴ p15

⁵ Cl. 5A.E.3(a) and 6.7A.1(b)

⁶ Cl. 6.8.2(c)

Example

The Distribution Network Service Provider might (for example) make separate connection charges for the provision of a connection asset and for making a necessary extension to, or other augmentation of, the distribution network

- (iii) the basis on which connection charges are determined; and
- (iv) the manner in which connection charges are to be paid (or equivalent consideration is to be given); and

Examples

The payment (or equivalent consideration) might take the form of a capital contribution, prepayment or financial guarantee.

- (v) a threshold (based on capacity or any other measure identified in the connection charge guidelines) below which a retail customer (not being a non-registered embedded generator or a real estate developer) will not be liable for a connection charge for an augmentation other than an extension.

Under clause 6.2.8(c) as amended, a regulatory proposal must include the proposed connection policy.

While the NER provides that the AER guidelines on the classification of distribution services and the control mechanisms for direct control services do not bind the AER, neither do they bind anyone else⁷. Therefore, notwithstanding the clause 6.7A.1(b) requirement for a connection policy to be consistent with the Guidelines, DNSPs are not bound by the Guideline.

Endeavour Energy notes that the Draft Guideline contemplates that connection services provided in a contestable market is likely to be classified as either a negotiated distribution service or an unclassified distribution service⁸.

Classifying a contestability regime as an unclassified distribution service would remove any likely inconsistency between the connection policy of a DNSP and the Draft Guideline.

To do otherwise would be to significantly increase regulatory uncertainty and undermines the regulatory proposal upon which a Distribution Determination is made.

Recommendation

A contestability regime is classified as an unclassified distribution service.

Negotiated and unclassified distribution services

As stated above, clause 6.2.8(a) of the NER provides that the AER may publish guidelines for the classification of distribution services and the control mechanisms for direct control services.

⁷ Cl. 6.2.8(a) and (c)

⁸ Clause 3.1.1, p9

Clause 6.2.8(a) of the NER would therefore appear to exclude from AER Guidelines the control mechanisms for distribution services other than direct control services. This includes the control mechanisms for negotiated distribution services and unclassified distribution services.

While Part C of Chapter 5A relating to negotiated connections, provides for a negotiated contract or aspects of such a contract, to be subject to Part C to the exclusion of the relevant provisions of Chapter 6, it does not appear to extend to the Guideline. This is consistent with the connection charge principle stated in clause 5A.E.1(c)(4) and the connection charging arrangements stated in clause 5A.C.3.

As such, and consistent with clause 6.2.8(c) of the NER, clause 3.1.2 of the Draft Guideline referring to charge requirements regardless of classification should be deleted. Further, in this context, the Draft Guidelines should not apply to negotiated and unclassified distribution services.

Recommendation

Unclassified distribution services be excluded from the Guideline;

Negotiated distribution services be excluded from the Guideline.

Method of determining charges for negotiated and unclassified services

In developing the guidelines, the AER must have regard to the historical and geographic differences between networks and the circumstances in which connection services may be provided by persons other than the DNSPs (and are therefore contestable)⁹.

Clause 3.1.1 of the Guideline provides that if the AER classifies a component of a connection service as a negotiated distribution service or does not classify the component of a connection, the cost of the connection service will be determined by the connection applicant and the relevant service provider.

Endeavour Energy supports the position stated in clause 3.1.1 of the Guideline.

Clause 3.1.2 of the Draft Guideline further provides that for negotiated or unclassified services, the charge must be agreed upon by the customer and the relevant service provider in accordance with the requirements of Chapter 5A, including the connection charge principles and the connection charge guideline¹⁰.

As an unclassified service, Chapter 5A and Chapter 6 do not apply. This exclusion of contestable services from the Guidelines reflects that the connection services agreement is made between the ASP and the customer, and is not enforced by either the DNSP or AER.

Recommendation

Amend references in the Guideline to state that for services classified as direct control services only, the charge should be in accordance with chapter 5A, including the connection charge principles and the connection charge guideline.

⁹ Clause 5A.E.3(e)

¹⁰ Clause 3.1.2, p9

Capital Contributions for Standard Control Services

The connection charge principles provide for a DNSP's connection policy to include a threshold below which a retail customer cannot be required to make a capital contribution towards the cost of an augmentation¹¹.

The threshold is determined by the DNSP, in accordance with the principles stated in the Draft Guideline. Where a connection policy is not approved by the AER, the AER has stated that it would set a network augmentation charge threshold at a maximum capacity of 100 Ampere 3 phase low voltage supply¹².

Where a retail customer applies for a connection service for which an augmentation is required, and the retail customer meets the relevant threshold, a DNSP may seek a capital contribution towards the cost of the augmentation.

The Draft Guideline sets out principles for determining incremental cost in calculating a capital contribution, including *"if a DNSP is able to use independent contracts to perform connection service work on its network, then the DNSP should offer to run a tender process on behalf of the connection applicant or allow a connection applicant to run a tender process, to procure the connection services."*¹³

Under NSW legislation, where a connection customer makes a capital contribution to an augmentation, they may elect an ASP to undertake the work and contract with the ASP directly. This connection contestability regime in NSW has operated successfully since 1995, providing timely and cost effective delivery of services to connection customers. The connection contestability regime also meets a fundamental purpose of the Guideline, being the provision, without undue administrative cost, of a user-pays signal to reflect the efficient cost of providing the connection services.¹⁴

Any application of the tendering arrangements set out in the Draft Guideline in NSW would be unnecessary, introduce inefficiencies, increase administrative costs for connection customers and would undermine the ASP Scheme, causing a contraction in the market for ASP services.

Recommendation

Where connection services are provided in a contestable market, the requirement for a DNSP to facilitate or implement a tender process in shared connection augmentations is to be deleted from the Guideline.

Treatment of augmentation assets

Clause 11.1.2 of the Guideline provides that any assets gifted to a DNSP by a connection applicant will not be included by the DNSP in the Regulated Asset Base (RAB).

The Guideline is contrary to both the NEL and current practice, whereby gifted assets are included by the DNSP in the RAB, albeit that they have a value of zero (consistent with the customer capital contribution being netted off the RAB).

¹¹ Cl. 5A.E.1(b)(2)

¹² Draft Guideline, p8

¹³ Draft Guideline, p12

¹⁴ Cl. 5A.E.3(b)(3)

The reason for the inclusion of gifted assets in the RAB, before the customer capital contribution is netted off, is for the asset to be recognised for maintenance and operating expense purposes.

The revenue and pricing principles¹⁵, provides for a regulated network service provider to be given a reasonable opportunity to recover at least the efficient costs the operator incurs in providing direct control services and complying with a regulatory obligation or requirement. Additionally, the revenue and pricing principles provide that regard should be had to the regulatory asset base with respect to a distribution system adopted in any previous distribution determination.

Excluding assets gifted to a DNSP by a connection applicant in the RAB would prevent a DNSP from being given reasonable opportunity to recover at least the efficient costs the operator incurs in providing direct control services.

Inclusion of the assets gifted to a DNSP by a connection applicant in the RAB would also reflect that when they are ultimately replaced by the DNSP, they would be included in the RAB at their full value.

Recommendation

The Guideline be amended to include assets gifted to a DNSP by a connection applicant in the Regulated Asset Base (RAB).

¹⁵ cl.7A of the National Electricity Law