04.01.02 – Jurisdictional Schemes

October 2014

Contents

1 Introduction

1.1 Overview

Jurisdictional schemes are certain programs implemented by State governments that place legislative obligations on distribution networks. Jurisdictional schemes include the schemes set out explicitly under clause 6.18.7A(e) of the National Electricity Rules (NER), as well as those determined by the Australian Energy Regulator (AER) to be jurisdictional schemes under clause 6.18.7A(l).

Under a jurisdictional scheme, a distribution network service provider, such as Ergon Energy, is obligated to pay an amount (the jurisdictional scheme amount), which may be a payment to a defined person; a payment into a fund established by a government; a credit against charges payable by a person; or a reimbursement paid to a specific person. The jurisdictional scheme amounts are subsequently recovered from customers through network charges.

In its regulatory determination, the AER must set out how we are to:

- report on the jurisdictional scheme amounts we recover from customers in order to provide for our obligations under these jurisdictional schemes; and
- adjust the jurisdictional scheme amounts we recover in subsequent years to account for any over or under recovery in prior years.[1]

1.2 Jurisdictional schemes in Queensland

Ergon Energy is currently subject to two jurisdictional schemes:

- Queensland Retailer of Last Resort Scheme, which places certain obligations on Ergon Energy in the event that a retailer within Ergon Energy's distribution area is suspended from trading under the NER or has its retail authority cancelled or suspended; and
- Queensland Solar Bonus Scheme, which obligates Ergon Energy to pay a feed-in-tariff for energy supplied into its distribution network from specific micro-embedded generators.

The following sections consider the application of the jurisdictional schemes in the 2015-2020 regulatory control period.

2 Retailer of Last Resort

There are provisions under both the National Energy Customer Framework (NECF)[2] and Part 3 of the *Electricity Regulation 2006* (Qld) (Electricity Regulation) to provide for the event that a commercial retailer of energy can no longer fulfil its obligations in the electricity market. These provisions enable another entity to assume some of the responsibilities of the failed retailer to seek to ensure continuity of supply of electricity to customers. These are known as Retailer of Last Resort (ROLR) schemes.

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[1] NER, clause 6.12.1(20)

[2] Part 6 of the National Energy Retail Law

The Queensland ROLR scheme under Part 3 of the Electricity Regulation was determined by the AER to be a jurisdictional scheme in March 2011.[3] This scheme obligates Ergon Energy to pay a person (the ROLR) an amount determined in accordance with its obligations under the scheme. This jurisdictional scheme amount is only payable if a ROLR event occurs and is to be an amount determined by the Queensland Competition Authority. Given the potential scale of a ROLR event, the amount cannot be reliably determined in advance of the ROLR event occurring.

Ergon Energy notes that the NECF provides a similar protection to customers. The NECF is expected to be implemented in Queensland by 1 July 2015, and it is assumed that the provisions of Part 6 of the National Energy Retail Law (which is one element of NECF) will apply in circumstances of a ROLR event. The NECF provides a national framework for the management of ROLR events and does not constitute a jurisdictional scheme. Furthermore, the ROLR provisions within Part 3 of the Electricity Regulation are expected to be repealed when the NECF legislation is enacted in Queensland.[4]

As this Queensland ROLR scheme will no longer apply from the start of the next regulatory control period, we have not set out how we propose to report to the AER on the recovery of jurisdictional scheme amounts.

3 Solar Bonus Scheme

3.1 Overview

The Solar Bonus Scheme (SBS) provides customers that have installed a solar photovoltaic (PV) generating system at their premises with a payment, known as the feed-in-tariff (FiT), for energy that they export into the Queensland electricity network. We are liable for the FiT payments made to customers under this scheme in our distribution area. The scheme operates under clause 44A of the *Electricity Act 1994* (Qld) and is recognised in clause 6.18.7A(e)(1) of the NER as a jurisdictional scheme.

The AER's distribution determination for 2010–2015 included FiT payments as part of the operating expenditure forecast and provided for Ergon Energy to recover any difference between our forecast FiT payments and actual FiT payments by way of a nominated pass through event.[5]

Due to the significantly greater than expected uptake of PV installations, there have been large differences between our 2010 forecasts of the annual payments under the scheme and the actual payments we have made to our customers. We have therefore submitted cost pass through applications to the AER to pass-through the difference in costs that we have incurred.

These pass-through amounts have been substantial. For example, in January 2014 the AER approved an extra $84 million ($Dec 2014) in FiT costs above our forecast to be passed through to consumers in the 2014–15 regulatory year.[6] This represented an increase in our annual revenue requirement for that year of approximately 5%.

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[3] AER, Letter to Energex, 8 March 2011. Note that this scheme applies to both Energex and Ergon Energy.

[4] Department of Energy and Water Supply, Queensland Government, http://www.dews.qld.gov.au/policies-initiatives/electricity-sector-reform/supply/customer-framework, updated 20 June 2014.

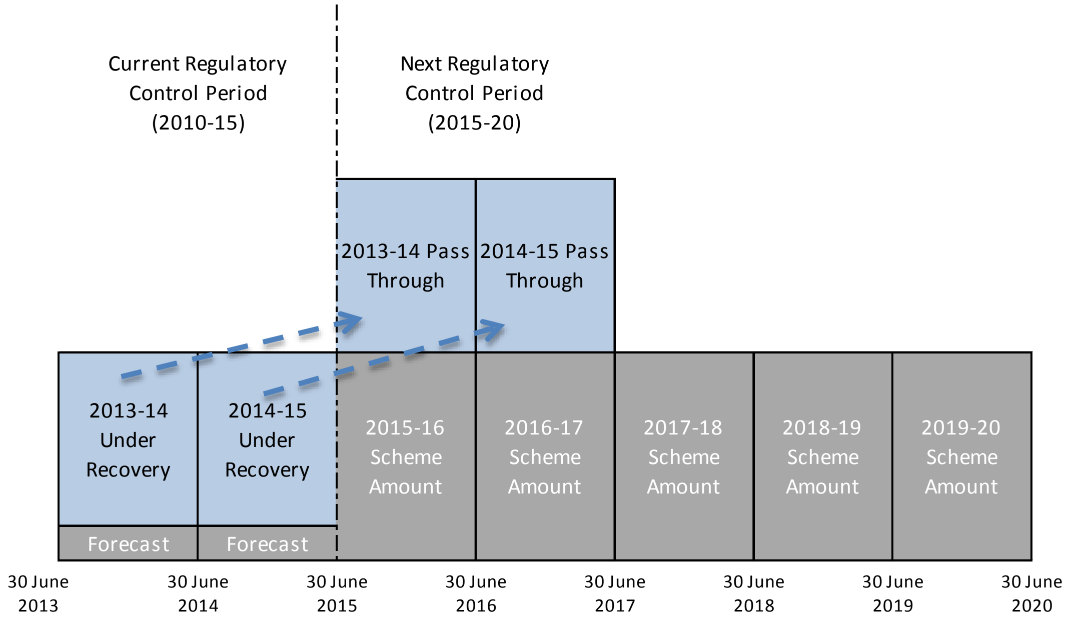
[5] AER, Final Decision: Queensland Distribution Determination, May 2010, pp. 311-312.

[6] AER, Determination: 2012–13 Queensland solar bonus scheme pass through for Ergon Energy, January 2014, p. 8.

In the next regulatory control period, we propose to recover FiT payments consistent with the NER provisions related to jurisdictional schemes.[7] This will result in us reporting on our FiT payments and their recovery from customers in our annual pricing proposals rather than through a nominated pass through event. This does not include, however, the remaining amounts to be recovered due to FiT payments made to customers in the 2013–14 and 2014–15 regulatory years, which will still be recovered via the nominated pass through mechanism, consistent with the current regulatory determination.

The change in the way the FiT payments are to be recovered has the potential to see a 'doubling up' of these costs on customers in the first two years of the next regulatory control period. That is, the excess of FiT payments over our 2010 forecasts (which is substantial) and the new and more accurate forecasts we have made in this proposal could be recovered, together, from customers in 2015–16 and 2016–17. We provide a graphical representation of this scenario in figure 1 below.

Figure 1: Feed-in tariff jurisdictional scheme recoveries and pass through recoveries under a 'standard' approach



To avoid this impost on customers we propose to delay the recovery of SBS amounts by two years throughout the next regulatory control period, and in the first two years of the 2020–2025 regulatory control period.

3.2 Proposed application of Solar Bonus Scheme

We propose to recover payments made to customers under the SBS with a two-year lag. For example, we would recover SBS amounts incurred by us in 2014–15 in 2016–17. We propose this approach to avoid the pricing impacts that would occur should we recover the pass through for SBS amounts incurred in the current regulatory control period in the same year as the total SBS scheme payments forecast for each year of the next regulatory control period.

[7] NER, clause 6.18.2(6A).

Our proposed approach has been selected from among a number of options, and we have undertaken customer consultation on these options.[8]

The options we have considered to moderate the effect of recovering SBS amounts on prices are as follows:

1. Recover the pass through amounts across multiple years of the next regulatory control period
2. Early adoption of the SBS as a jurisdictional scheme and removal of the pass through arrangements
3. Smoothing the 2015–16 and 2016–17 jurisdictional scheme amounts over multiple years of the regulatory control period
4. Delayed recovery of jurisdictional scheme amounts (our proposed option).

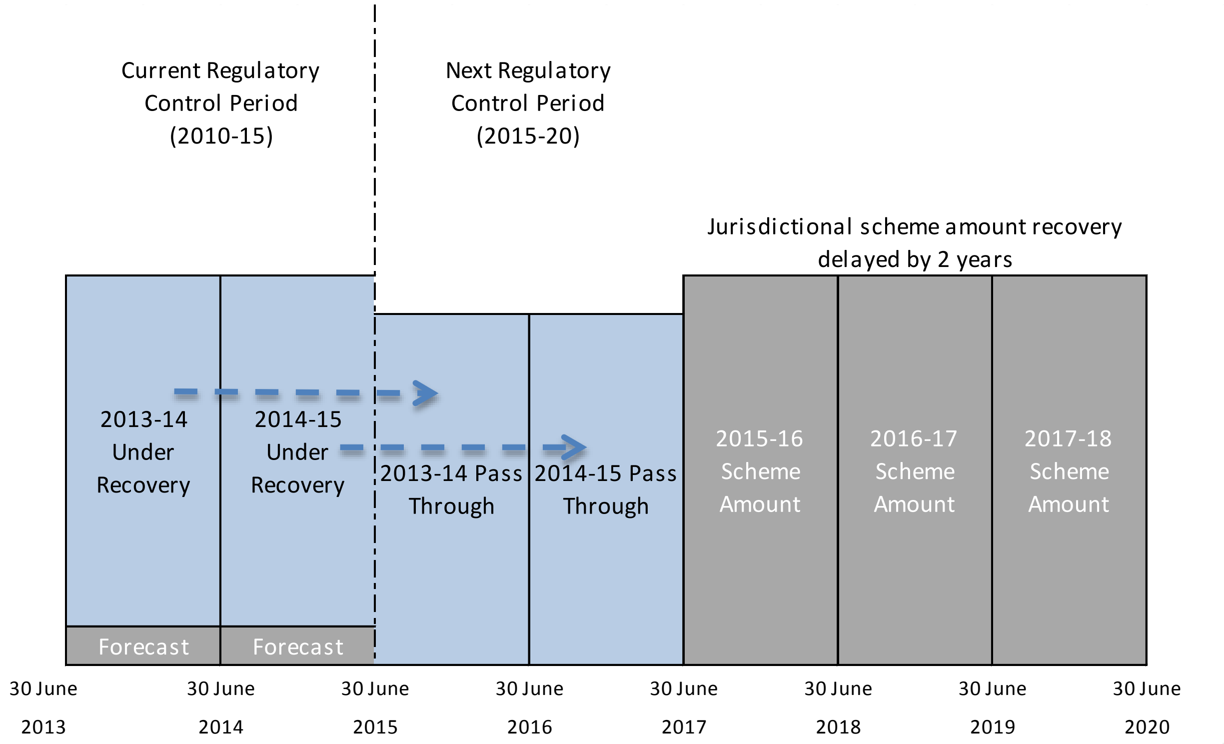
We have disregarded option 2 because we consider that this would have required revocation and substitution of Ergon Energy's current revenue determination.

Options 1 and 3 are both conceptually more complex and require more detailed modelling of payments and prices in order to smooth out the price impacts to consumers. Our preferred option is option 4, which is administratively simpler. This option is also the approach that we consider would be accepted by our customers, based on customers' views expressed during our consultation processes on this matter.[9] We provide a graphical illustration of option 4 below.

[8] The options for the recoveries of the FiT costs were presented and discussed at the Customer Council AER2015 Working Group meeting in April 2014. Further information, including a copy of the presentation, is provided in: Ergon Energy, *Customer Council AER2015 Working Group*, April Communique Suite, April 2014, https://www.ergon.com.au/__data/assets/pdf_file/0018/204741/140507-Council-Working-Group-Notes-and-Presentations-April-2014.pdf.

[9] Ergon Energy, Customer Council AER2015 Working Group Meeting Notes, May 2014, The issue was first raised in the April 2014 Working Group meeting and then discussed further in the May 2014 meeting. A copy of the Working Group Meeting notes is available here: https://www.ergon.com.au/__data/assets/pdf_file/0018/206910/140519-Customer-Council-AER2015-Working-Group-Meeting-Notes.pdf

Figure 2: Recovery of jurisdictional scheme amounts with a two-year lag (option 4)



Our proposed approach is consistent with the rules regarding the recovery of jurisdictional scheme amounts. Clause 6.18.7A of the NER states that we must:

- set our tariffs such that we can recover the jurisdictional scheme amounts; and
- ensure that in any given regulatory year, we do not pass on to customers through our tariffs an amount that exceeds the estimated costs of the jurisdictional scheme, modified for any over or under recovery.

In our proposed approach, we would not seek to recover the costs of the SBS from customers in the year those costs are incurred. Rather, we would only recover those costs from customers two years after the cost have been incurred as shown in Figure 2 above.

We believe this is consistent with the NER as clause 6.18.7A does not require the costs incurred under the jurisdictional scheme to be passed onto customers in the same year in which we incur them. Furthermore, the requirement in clause 6.18.7A(b) is that the amount to be passed on *"must not exceed"* the sum of the estimated amount and the under or over adjustment, adjusted as appropriate to account for the cost of capital. A value of $0 in the year in which the FiT cost is incurred and the balance of the jurisdictional scheme amount two years later (adjusted for WACC to account for cost of capital) is consistent with this requirement.

We also note that protecting customers from the price implications of recovering both a FiT cost pass through an SBS jurisdictional scheme amount in a single year would be consistent with the National Electricity Objective.[10] Assuming Ergon Energy is compensated for the delay in recovering the costs of the SBS by an appropriate rate of return adjustment over the lag period, our proposed approach would ensure that we are compensated for the efficient costs that we incur.

[10] National Electricity Law, section 7.

3.3 Forecast payments under the Solar Bonus Scheme

In order to forecast payments under the SBS, we take a number of factors into account. First and foremost, we consider the number of existing inverter energy system (IES) meter service orders that we have closed off in our financial reporting system. We take into account the mean size of the installed solar arrays and historical monthly export in kWh per unit of installed capacity. This allows us to take into account seasonal changes in energy exports.[11] For internal business purposes, we forecast best case, high case, and low case scenarios for energy exports. The forecasts we have provided in this attachment are our "best case" forecasts.

Table 1 table sets out the forecast payments under the Solar Bonus Scheme during the 2015-2020 regulatory control period.

Table 1: Forecasts of Solar Bonus Scheme-related items, 2015-2020[12]

	2015-16	2016-17	2017-18	2018-19	2019-20
Feed-in Tariff Payments ($m nominal)	109.8	107.6	104.9	102.1	99.2
Installed capacity (kW)	253,447	247,960	242,131	236,041	229,750
Energy exported (GWh)	249.7	244.5	238.9	233.1	227.1

Under the proposed recovery mechanism, there will be no impact to customers from a difference between our forecast of SBS payments and actual payments made. This is because we will only recover payments made with a two year lag, which means that audited outturn figures will be available when these amounts are included in network charges.

3.4 Annual reporting

We are required by the NER to specify how jurisdictional scheme amounts are to be recovered from customers in our annual pricing proposal and how we will adjust tariffs resulting from under or over recovery of jurisdictional scheme amounts.[13]

We will set out in our annual pricing proposal:

- the jurisdictional scheme amounts that we will recover from customers for the relevant regulatory year; and
- how those amounts will be passed on to customers.

Consistent with our proposed two year lag, actual FiT payments made in Year t will be recovered in Year t+2. The amount to be recovered will be adjusted for the time cost of money by applying the relevant WACC for the two years of the lag between when we incur the cost and when we recover those costs from our customers. This will ensure that Ergon Energy does not recover more (or less) than the costs it actually incurs.

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[11] Further information on our approach to forecasting installed PV capacity and FiT payments is set out in Ergon Energy's *07.02.12 - Distribution Network Impacts of Photovoltaic Connections to 2020*.

[12] Based on forecasts provided to the QCA in July 2014 and set out in *06.02.05 - Ergon Energy: Letter to the QCA Projected Costs of the Solar Bonus Scheme*. Updates to forecasts have been made since this time and incorporated into our forecasts of jurisdictional scheme recoveries in Table 2 below.

13 NER, clause 6.18.2(b)(6A).

3.5 Impact on Regulatory Proposal

Table 3 sets out the forecast jurisdictional scheme amounts included in the total allowable revenue. We have calculated the jurisdictional scheme amounts based on our forecasts (as discussed in section 3.2 above) and adjusted for the time cost of money. These are the amounts that will be added to our total allowed revenue.

Table 2: Solar Bonus Scheme – Jurisdictional Scheme Amounts, 2015-2020[14]

	2015-16	2016-17	2017-18	2018-19	2019-20
Forecast Feed-in Tariff Payments ($m nominal)	110.4	106.8	104.9	102.1	99.2
Forecast WACC	8.02%	8.02%	8.02%	8.02%	8.02%
Proposed recovery of jurisdictional jcheme amounts – Solar Bonus Scheme	0.0	0.0	128.8	124.6	122.4

The above estimate is based on forecast WACC of 8.02%. The actual jurisdictional scheme amounts to be recovered from our customers will be based on the applicable WACC in each year, consistent with our proposed approach for determining the WACC as set out in Appendix D of our Regulatory Proposal.

The above table does not include the forecast recovery of the feed-in tariff payments resulting from under-recovery of the costs of the actual FiT in the current regulatory control period. Those amounts will be subject to pass through applications, which will be assessed separately by the AER.

14 Based on latest information available at the time of finalising our forecasts for the Regulatory Proposal (September 2014). These figures differ to the forecasts set out in Table 1 of this attachment. Ergon Energy will provide updated feed-in-tariff forecasts to the AER at the time of our Revised Proposal.