



Ergon Energy
draft distribution determination
2010–11 to 2014–15

25 November 2009

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Summary

Clause 6.11.1 of the National Electricity Rules (NER) requires the Australian Energy Regulator (AER) to make a distribution determination in relation to Ergon Energy.

Under clause 6.12.1 of the NER, this distribution determination is predicated on the following constituent decisions:

- (1) a decision on the classification of the services to be provided by the Distribution Network Service Provider during the course of the regulatory control period;
- (2) a decision on the Distribution Network Service Provider's current building block proposal in which the AER either approves or refuses to approve:
 - (i) the annual revenue requirement for the provider, as set out in the building block proposal, for each regulatory year of the regulatory control period; and
 - (ii) the commencement and length of the regulatory control period as proposed in the building block proposal;
- (3) a decision in which the AER either:
 - (i) acting in accordance with clause 6.5.7(c), accepts the total of the forecast capital expenditure for the regulatory control period that is included in the current building block proposal; or
 - (ii) acting in accordance with clause 6.5.7(d), does not accept the total of the forecast capital expenditure for the regulatory control period that is included in the current building block proposal, in which case the AER must set out its reasons for that decision and an estimate of the total of the Distribution Network Service Provider's required capital expenditure for the regulatory control period that the AER is satisfied reasonably reflects the capital expenditure criteria, taking into account the capital expenditure factors;
- (4) a decision in which the AER either:
 - (i) acting in accordance with clause 6.5.6(c), accepts the total of the forecast operating expenditure for the regulatory control period that is included in the current building block proposal; or
 - (ii) acting in accordance with clause 6.5.6(d), does not accept the total of the forecast operating expenditure for the regulatory control period that is included in the current building block proposal, in which case the AER must set out its reasons for that decision and an estimate of the total of the Distribution Network Service Provider's required operating expenditure for the regulatory control period that the AER is satisfied reasonably reflects the operating expenditure criteria, taking into account the operating expenditure factors;
- (5) a decision in relation to the rate of return on whether to apply or depart from a value, method or credit rating level set out in a statement of regulatory intent in accordance with clause 6.5.4;

- (6) a decision on the regulatory asset base as at the commencement of the regulatory control period in accordance with clause 6.5.1 and schedule 6.2;
- (7) a decision on the estimated cost of corporate income tax to the provider for each regulatory year of the regulatory control period in accordance with clause 6.5.3 and, where relevant, a statement of regulatory intent under clause 6.5.4;
- (8) a decision on whether or not to approve the depreciation schedules submitted by the Distribution Network Service Provider and, if the AER decides against approving them, a decision determining depreciation schedules in accordance with clause 6.5.5(b);
- (9) a decision on how any applicable efficiency benefit sharing scheme, service target performance incentive scheme, or demand management incentive scheme is to apply to the Distribution Network Service Provider;
- (10) a decision in which the AER decides other appropriate amounts, values or inputs;
- (11) a decision on the control mechanism (including the X factor) for standard control services (to be in accordance with the relevant framework and approach paper);
- (12) a decision on the control mechanism for alternative control services (to be in accordance with the relevant framework and approach paper);
- (13) a decision on how compliance with a relevant control mechanism is to be demonstrated;
- (14) a decision on the additional pass through events that are to apply for the regulatory control period;
- (15) a decision on the negotiating framework that is to apply to the Distribution Network Service Provider for the regulatory control period (which may be the negotiating framework as proposed by the provider, some variant of it, or a framework substituted by the AER);
- (16) a decision in which the AER decides the Negotiated Distribution Service Criteria for the Distribution Network Service Provider;
- (17) a decision on the procedures for assigning customers to tariff classes, or reassigning customers from one tariff class to another (including any applicable restrictions);
- (17A) a decision on the approval of the proposed pricing methodology for transmission standard control services (if rule 6.26 applies);
- (18) a decision on whether depreciation for establishing the regulatory asset base as at the commencement of the following regulatory control period is to be based on actual or forecast capital expenditure;
- (19) a decision on how the Distribution Network Service Provider is to report to the AER on its recovery of Transmission Use of System charges for each regulatory year of the regulatory control period and on the adjustments to be made to subsequent pricing proposals to account for over or under recovery of those charges.

In addition to the constituent decisions in clause 6.12.1, the NER sets out the following requirements for the distribution determination:

- Clause 6.3.2(a) requires the AER to make a building block determination in relation to ETSA Utilities, as a component of a distribution determination. The building block determination is to specify the following matters for a regulatory control period:
 - (1) the Distribution Network Service Provider's annual revenue requirement for each regulatory year of the regulatory control period;
 - (2) appropriate methods for the indexation of the regulatory asset base;
 - (3) how any applicable efficiency benefit sharing scheme, service target performance incentive scheme, or demand management incentive scheme are to apply to the Distribution Network Service Provider;
 - (4) the commencement and length of the regulatory control period;
 - (5) any other amounts, values or inputs on which the building block determination is based (differentiating between those contained in, or inferred from, the service provider's building block proposal and those based on the AER's own estimates or assumptions).

- Clause 6.12.3(a) of NER allows the AER the discretion to accept or approve, or refuse to accept or approve any element of a regulatory proposal.

- Clause 6.12.3(f) of the NER requires that if the AER refuses to approve an amount or value referred to in clause 6.12.1, the substitute amount or value on which the distribution determination is based must be:
 - (1) determined on the basis of the current regulatory proposal; and
 - (2) amended from that basis only to the extent necessary to enable it to be approved in accordance with the Rules.

The AER's draft decisions for Erson Energy's draft distribution determination are set out below. Detailed analysis and discussion of the AER's considerations and reasoning is set out in the AER's draft decision, released with this draft determination. Reference to the draft decision is a reference to the AER's draft decision released with this determination on 30 November 2009, entitled *Draft decision, Queensland draft distribution determination 2010–11 to 2014–15*, 25 November 2009. Abbreviations have the meaning given to them in the draft decision.

Draft determination – constituent decisions

In accordance with clause 6.12.1(1) of the NER, the classification of services as set out in appendix A of the draft decision will apply to Ergon Energy for the next regulatory control period.

In accordance with clause 6.12.1(2)(i) of the NER, the AER refuses to approve the annual revenue requirement proposed by Ergon Energy.

In accordance with clauses 6.12.1(2)(ii) and 6.3.2(a)(4) of the NER, Ergon Energy's regulatory control period is from 1 July 2010 to 30 June 2015.

In accordance with clause 6.12.1(3)(ii) of the NER the AER does not accept Ergon Energy's forecast capex for the next regulatory control period. The AER is not satisfied that Ergon Energy's forecast capex, taking into account the capex factors, reasonably reflects the capex criteria in clause 6.5.7 of the NER.

The AER's reasons for this decision are set out in section 7.8 of the draft decision.

The AER's estimate of the total capex required by Ergon Energy in the next regulatory period, that reflects the capex criteria taking into account the capex factors, is set out in table 7.7 of the draft decision.

In accordance with clause 6.12.1(4)(ii) of the NER, the AER does not accept Ergon Energy's proposed forecast opex for the next regulatory control period. The AER is not satisfied that Ergon Energy's forecast opex, taking into account the opex factors, reasonably reflects the opex criteria in clause 6.5.6 of the NER.

The AER's reasons are set out in section 8.8 of the draft decision.

The AER's estimate of Ergon Energy's required opex for the next regulatory control period, that reflects the opex criteria taking into account the opex factors, is set out at table 8.27 of the draft decision.

In accordance with clause 6.12.1(5) of the NER, the rate of return to apply to Ergon Energy is 10.06 per cent.

In accordance with clause 6.12.1(6) of the NER the opening asset base for Ergon Energy as at 1 July 2010 is \$7105.4 million.

In accordance with clause 6.12.1(7) of the NER the estimated cost of corporate tax to Ergon Energy for each regulatory year of the next regulatory control period is as specified in table 9.3 of the draft decision.

In accordance with clause 6.12.1(8) of the NER the AER has not accepted the depreciation allowances submitted by Ergon Energy. The AER has determined the depreciation allowances for Ergon Energy set out in table 10.4 of the draft decision.

In accordance with clause 6.12.1(9) of the NER, the AER has determined that the national distribution STPIS will apply to Ergon Energy in the next regulatory control period in the following form:

1. the applicable component and parameters are the SAIDI and SAIFI reliability of supply parameters. The AER will apply the telephone answering customer service parameter to Ergon Energy
2. overall revenue at risk is ± 2 per cent and ± 0.2 per cent for the telephone answering parameter
3. the incentive rates to apply to each applicable parameter were calculated in accordance with clauses 3.2.2, 5.3.2(a)(1) and appendix B of version 01.2 of the STPIS, as set out in table 12.5 of the draft decision
4. that the performance targets to apply to each applicable parameter in each regulatory year of the next regulatory control period as set out at table 12.7 of the draft decision
5. the GSL component will not apply while the QCA's GSL scheme remains in place. In the event that the QCA's GSL scheme is withdrawn the AER will implement such a scheme from the day the jurisdictional scheme is withdrawn.

In accordance with clause 6.12.1(9) of the NER, the EBSS to apply to Ergon Energy is as set out in the AER's *Final Framework and approach paper, Application of schemes, Energex and Ergon Energy 2010–15*, published in November 2008.

The following opex cost categories will be excluded from the operation of the EBSS for the next regulatory control period:

- debt raising costs
- insurance and self insurance costs
- superannuation costs for defined benefits and retirement schemes
- the demand management innovation allowance.

These excluded costs will be recognised in addition to the adjustments and exclusions set out in section 2.3.2 of the EBSS, which include non-network alternatives and recognised pass through events.

In accordance with clause 6.12.1(9) of the NER, the DMIS to apply to Ergon Energy is the DMIS set out in the AER's document, *Demand management incentive scheme - Energex, Ergon Energy and ETSA Utilities 2010–15*, October 2008.

The AER decides that Part A of the DMIS (that is, the DMIA) will apply to Ergon Energy. The DMIA is capped at \$5 million for the next regulatory control period and allocated to Ergon Energy in equal annual instalments of \$1 million for each year of the next regulatory control period, as specified in section 14.6 of the draft decision.

In accordance with clause 6.12.1(10) the other appropriate amounts, values or inputs to be input to the PTRM for Ergon Energy are the AER maximum demand and customer number forecasts specified in table 6.12 of the draft decision.

In accordance with clause 6.12.1(11) of the NER, the X factors to apply to Ergon Energy are as specified in table 16.12 of the draft decision.

In accordance with clause 6.12.1(11) of the NER, the control mechanism for standard control services provided by Ergon Energy is a revenue cap.

The revenue cap for any given regulatory year is the MAR for that regulatory year (as calculated using the formula in section 4.6.1 of the draft decision) plus any unders/overs adjustment required to get the DUOS under/overs account (as set out in appendix D to the draft decision) to zero (or the agreed tolerance level).

The side constraints to apply to the price movements of each of Ergon Energy's tariff classes must be consistent with the formula in section 4.6.2 of the draft decision.

In accordance with clause 6.12.1(12) of the NER, the control mechanisms to apply to Ergon Energy's quoted services are:

- caps on the prices of indicative individual services in the first regulatory year of the next regulatory control period
- price paths, set out in table 18.10, for the remaining regulatory years of the next regulatory control period.

In accordance with clause 6.12.1(12) of the NER, the control mechanisms to apply to Ergon Energy's fee based services are:

- caps on the prices of individual services in the first regulatory year of the next regulatory control period
- price paths, set out in appendix P of the draft decision, for the remaining years of the next regulatory control period.

In accordance with clause 6.12.1(12) of the NER, the control mechanism to apply to Ergon Energy's street lighting services is:

- caps on the prices of individual services in the first regulatory year of the next regulatory control period (as set out in table 17.18 of the draft decision)
- price paths, as set out in table 17.18 of the draft decision, for the remaining regulatory years of the next regulatory control period.

In accordance with clause 6.12.1(13) of the NER, Ergon Energy's compliance with the control mechanism for street lighting services is to be demonstrated through the annual pricing approval process. The process for demonstrating compliance is specified in section 17.6.4 of the draft decision.

In accordance with clause 6.12.1(13) of the NER, Ergon Energy's compliance with the control mechanism for quoted services and fee based services is to be demonstrated through the annual pricing approval process. The process for demonstrating compliance is specified in section 18.6.4 of the draft decision.

In accordance with clause 6.12.1(13) of the NER, Ergon Energy must demonstrate compliance with the control mechanism for standard control services in accordance with appendices D and E of the draft decision.

In accordance with clause 6.12.1(14) of the NER, the additional pass through events that apply to the Qld DNSPs for the next regulatory control period are the:

- smart meter event
- CPRS event
- feed-in tariff event
- general nominated pass through event

as defined in section 15.7 of the draft decision.

In accordance with clause 6.12.1(16) of the NER, the NDSC to apply to Ergon Energy for the next regulatory control period are in appendix C of the draft decision.

In accordance with clause 6.12.1(17) of the NER, the procedures to be applied by the Qld DNSPs for assigning customers to tariff classes or reassigning customers from one tariff class to another are specified in appendix B of the draft decision.

In accordance with clause 6.12.1(18) of the NER, the AER has decided to use actual depreciation for establishing the regulatory asset base for the commencement of the 2015–20 regulatory control period.

In accordance with clause 6.12.1(19) of the NER, Ergon Energy must submit, as part of its annual pricing proposal, a record of the amount of revenues recovered from TUOS charges and associated payments in accordance with appendix E of the draft decision.

Building block determination

In accordance with clause 6.3.2(a)(1) of the NER, Ergon Energy's annual revenue requirement for each regulatory year of the next regulatory control period is as set out in table 16.12 of the draft decision.

In accordance with clause 6.3.2(a)(2) of the NER, an appropriate methodology for indexation of Ergon Energy's regulatory asset base is as specified in section 16.5.3 of the draft decision.

In accordance with clause 6.3.2(a)(3) of the NER, the EBSS to apply to the Qld DNSPs is as specified in section 13.6 of the draft decision.

In accordance with clause 6.3.2(a)(4) of the NER, the regulatory control period is from 1 July 2010 to 30 June 2015.

In accordance with clause 6.3.2(a)(5) of the NER, any other amounts, values or inputs on which Ergon Energy's building block determination is based are as specified in sections 16.5 and 16.6 of the draft decision.