

14 October 2014

Mr Chris Pattas
General Manager
Network Investment and Pricing
Australian Energy Regulator
GPO Box 520
Melbourne Vic 3001

Dear Mr Pattas

Vegetation management cost pass through - implementation of AER deemed determination

I am writing in regard to the implementation of the AER's deemed determination pursuant to clause 6.6.1(e) of Transitional Chapter 6 of the National Electricity Rules (**Rules**) in respect of ActewAGL Distribution's application of November 2013 titled *Vegetation management cost pass through (Application)*.¹

In correspondence between the legal representatives for ActewAGL Distribution and the AER in ACT 2 of 2014 and Federal Court Proceeding No VID447/2014, ActewAGL Distribution and the AER agreed that the effect of clause 6.6.1(e) of Transitional Chapter 6 is that the AER is taken to have accepted ActewAGL Distribution's Application and that the manner in which the AER would give effect to the deemed determination (including the amount to be recovered, the regulatory year(s) in which recovery would occur and any consequential effects, such as the impact on incentive mechanisms) would be determined by agreement as between the AER and ActewAGL Distribution.² I understand that there have been some preliminary discussions between my staff and yours on the manner of implementation of the deemed determination, in which it was agreed that ActewAGL Distribution would send a proposal to the AER. This letter sets out ActewAGL Distribution's proposal for the AER's consideration.

Clause 6.6.1(e) of Transitional Chapter 6 provides that the AER is taken to have determined that:

- the positive pass through amount as proposed in the Application is the approved pass through amount; and
- the amount of that approved pass through amount that should be passed through to distribution network users in the regulatory year in which, and each regulatory year after

¹ Transitional Chapter 6 is Chapter 6 of the Rules in the form set out in Appendix 1 to the NER (clause 11.15.2(f)). Pursuant to Division 2 of Part M of Chapter 11 of the Rules, Transitional Chapter 6 applied to the making of the AER's determination in respect of ActewAGL Distribution's Application (see clause 11.15.2, in particular paragraph (a)).

² Letter from DLA Piper to Corrs Chambers Westgarth (**Corrs**) dated 15 August 2014, Corrs' letter of reply dated 18 August 2014, email correspondence between Fleur Gibbons of DLA Piper and Frances Williams of Corrs on 18 and 19 August 2014 and DLA Piper's letter to Corrs dated 20 August 2014.

that in which, the positive change event occurred, is as proposed by ActewAGL Distribution in that Application.

The positive pass through amount proposed in ActewAGL Distribution's Application was \$2,198,413.94 (\$2012/13), comprised of vegetation management expenditure of \$1,857,511.52 (\$2012/13) and a time cost of money premised on pass through occurring in the 2014/15 regulatory year of \$340,902.42.³ Notwithstanding that, strictly, this positive pass through amount is the approved pass through amount, ActewAGL Distribution proposes that the amount to be recovered reflect the revision to its proposed positive pass through amount proposed by ActewAGL Distribution in December 2013 to correct minor calculation errors.⁴ This revised proposed positive pass through amount is \$2,193,438.70 (\$2012/13), comprised of \$1,853,307.77 (\$2012/13) for vegetation management expenditure and a time cost of money premised on pass through occurring in the 2014/15 regulatory year of \$340,130.92.⁵

In its Application, ActewAGL Distribution proposed that the positive pass through amount be passed through to distribution network users in full in the 2014/15 regulatory year.⁶ However, as the AER approved ActewAGL Distribution's pricing proposal for the 2014/15 regulatory year in accordance with clause 6.18.8 of the Rules on 12 June 2014, ActewAGL Distribution proposes, and understands that the AER is agreeable to, the pass through to distribution network users of the approved pass through amount in full in the 2015/16 regulatory year.

ActewAGL Distribution proposes that this be achieved through the AER's constituent decision on the formulae to give effect to the control mechanism for standard control services to be made in its forthcoming distribution determination for ActewAGL Distribution for the subsequent regulatory control period. The control mechanism for ActewAGL Distribution's standard control services proposed in the AER's Stage 1 Framework and Approach paper for ActewAGL Distribution includes a B_t term which is defined as:

*"the sum of annual adjustments in year t. To be decided in the final decision."*⁷

ActewAGL Distribution proposes that the AER exercise its discretion under the Rules to define the B_t term such that it provides for the recovery of the deemed approved pass through amount. Specifically, ActewAGL Distribution proposes that the AER, in making its distribution determination for ActewAGL Distribution for the subsequent regulatory control period, define the B_t term, where year t is the 2015/16 regulatory year, to include approved pass through amounts relating to regulatory year t-1 (i.e. 2014/15) determined by the AER in accordance with clause 6.6.1 of Transitional Chapter 6 but not recovered in that regulatory year t-1 adjusted for the time cost of money. As the time cost of money included in the deemed approved pass through amount in respect of ActewAGL Distribution's Application is premised on recovery occurring in the 2014/15

³ ActewAGL Distribution's Application, see in particular p. 21 and the excel spreadsheet included as an attachment to that Application.

⁴ ActewAGL Distribution's *Vegetation management cost pass through: Additional information* dated December 2013 provided to the AER under cover of a letter dated 19 December 2013 in response to the AER's information request dated 2 December 2013 (**December Information Response**).

⁵ Attachment A to ActewAGL Distribution's December Information Response, excel workbook titled 'Corrected attachment to initial submission'.

⁶ ActewAGL Distribution's Application, p. 21.

⁷ AER 2013, *Stage 1 Framework and Approach ActewAGL*, p. 38

regulatory year, the B₁ term should be defined such that that approved pass through amount is adjusted to reflect the additional time value of money associated with the 12 month delay in recovery. ActewAGL Distribution proposes that this adjustment applies the allowed rate of return determined by the AER for the relevant regulatory year.

We note that, in correspondence with ActewAGL Distribution's legal representative, the AER's legal representative referred to the AER taking steps to ensure that ActewAGL's revenue allowance is changed to include the deemed approved pass through amount.⁸ We have concerns that an adjustment to the revenue allowance in the manner proposed may not be consistent with the Rules. We therefore propose the recovery through the B₁ term in the control mechanism for standard control services for the subsequent regulatory control period.

The vegetation management expenditure included in the approved pass through amount (i.e. \$1,853,307.77 (\$2012/13)) should be excluded from actual operating expenditure for the 2012/13 regulatory year in calculating the revenue increments / decrements for the transitional and subsequent regulatory control periods arising from the application of the Efficiency Benefit Sharing Scheme (EBSS) in the 2009-14 regulatory control period.

Given that our proposal involves an adjustment via one of the terms in the control mechanism for standard control services to apply in the subsequent regulatory control period to be decided in the AER's final decision on the ACT distribution determination for that period, ActewAGL Distribution observes that it is desirable that the manner of implementation of the AER's deemed determination is resolved in sufficient time to be reflected in the AER's forthcoming draft determination to be published in late November.

We look forward to hearing the AER's views at the earliest opportunity. Our contact for this matter is Leanne Holmes, Manager Economic Regulation. Leanne can be contacted on 0412 850715.

Yours sincerely



Stephen Devlin
General Manager
Asset Management

⁸ Corrs' letter to DLA Piper dated 18 August 2014 and email from Frances Williams of Corrs to Fleur Gibbons of DLA Piper on 19 August 2014.