



13 February 2015

Mr Warwick Anderson
General Manager - Networks Branch
Australian Energy Regulator
GPO Box 3131
Canberra ACT 2601

Dear Mr Anderson

RE: SUBMISSION TO AER DRAFT DETERMINATION FOR NSW ELECTRICITY DISTRIBUTORS

Origin Energy Electricity Limited (ABN 33 071 052 287, “Origin”) appreciates the opportunity to provide a response to the Australian Energy Regulator’s (AER) Draft Decision with respect to the determination of regulatory revenue allowances for the New South Wales (NSW) electricity distribution businesses for the period 2014-15 to 2018-19.

The AER’s decision is the first determination following changes to the National Electricity Law and National Electricity Rules in 2012. As a result, the AER has adopted a more holistic approach to decision making where it approves total expenditure allowances, not programs or projects. Under this approach, it is a matter for a distribution network service provider (DNSPs) to decide how and when it will spend its revenue allowance to run its network.

Origin agrees in principle with the approach taken by the AER to adopt a less prescriptive and granular approach to assess proposed costs and delegate greater responsibility to the businesses on how they manage their revenue allowances.

Despite a lessening of network performance standards, and historically lower than expected system demand, the costs proposed by the DNSPs are well above the historic trend. Furthermore, the AER’s benchmark modelling has revealed the NSW businesses were the least productive in the National Electricity Market. In light of this, Origin supports the alternative forecasts of operating and capital expenditure made by the AER.

As raised by Origin previously, the lack of an orderly presentation of information by the NSW DNSPs has been a significant concern. The AER and its consultants have identified systemic failings undermining the prudence of the proposed capital expenditure, most notably the lack of robust information and analysis.

For these reasons, Origin is strongly of the view that the onus must be on the businesses to demonstrate that any revised proposal is underpinned by prudent systems, consistent with good operating practice, and that these systems are using robust and reliable data. Where this is not made available, Origin considers that the AER’s alternative program better reflects the capex criteria set out in the National Electricity Rules.

However, Origin is concerned that while the AER has found the businesses to be materially inefficient, Ausgrid remains entitled to \$260.3M and Endeavour \$93.4M in efficiency benefits resulting from their performance in the previous regulatory period. In our view, these rewards are disproportionate compared to the costs faced by consumers to fund the DNSPs’ operational inefficiencies over 2009-2014.

In terms of the AER's approach to the weighted average cost of capital (WACC) and the transition to a trailing average cost of debt, Origin considers that the approach proposed by the businesses seeks to lock-in the accumulated global financial crisis benefit before any reversal can take effect. We also consider there is insufficient evidence to support the assertion that a transition to a trailing cost of debt approach is inconsistent with the National Electricity Rules or that it will not provide the DNSPs with an opportunity to recover at least their efficient financing costs. The AER has adopted a balanced and pragmatic approach that provides certain and predictable outcomes for investors and provides a balance between the views of consumer groups and the DNSPs.

Finally, Origin considers the AER's revised position to remove exit fees for customers switching to an unregulated meter is consistent with the objectives of the Australian Energy Market Commission's Power of Choice Review and will encourage competition in metering and related services. Origin also encourages the AER to ensure the annual metering charges for existing meters are set at a level that is compatible with supporting entry into the market for meter provision which will promote innovation and increase the range of services that could be offered to customers.

If you have any questions regarding this submission please contact Sean Greenup in the first instance on (07) 3867 0620.

Yours sincerely

A handwritten signature in blue ink that reads "K. Robertson". The signature is written in a cursive style.

Keith Robertson
Manager, Wholesale and Retail Regulatory Policy
(02) 9503 5674 keith.robertson@originenergy.com.au



*Response to AER Draft Determination NSW DNSPs for the
regulatory control period 2014-19*

Origin Submission

February 2015

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1 Opex

1.1 Summary

- Support the AER's application of the Expenditure Forecast Assessment Guideline to estimate an alternative base opex on the basis the costs proposed by the NSW DNSPs were acknowledged to be above efficient levels.
- Support the AER's decision to recognise general limitations of the benchmarking model. The AER's adjustments result in a balanced decision that reflects both the degree of existing inefficiencies in the DNSPs while at the same time providing an allowance that a prudent operator would require to achieve the operating expenditure objectives.
- Agree that the DNSPs' reform programs are only needed because they are not currently operating as efficiently as they could and these should therefore not be allowed as step changes.
- Strongly opposed to consumers having to continue to fund the inefficient costs of the DNSPs until they are able to transition to efficient levels. Any transition must be borne by the DNSPs, not consumers.

1.2 Base Opex

Background

Under the AER's base step trend method, the revealed costs for 2012-13 were used as the base year for forecast operating expenditure (opex).

Each of the NSW DNSPs proposed a base level of opex primarily on the actual opex they incurred in 2012-13, despite acknowledging these were above efficient levels.¹

In Origin's response to the NSW DNSPs' regulatory proposals, we were particularly concerned about inefficient labour costs that were embedded in the base year costs and the risk of the starting point entrenching inefficiencies.

AER's Draft Decision

The AER estimated that the base year opex proposed by Ausgrid, Endeavour Energy and Essential Energy were materially inefficient, driven primarily by inefficient labour and workforce management costs. As such, it sought to establish an alternative opex to set a more efficient base. The alternative base opex determined by the AER is significantly lower than the base opex proposed by the NSW DNSPs. The final differences between the AER alternative values and the base opex proposed by Ausgrid, Endeavour and Essential were 33.3%, 10.3% and 34.7% respectively.

The AER's assessment approach was consistent with its Expenditure Forecast Assessment Guideline (the Guideline). The approach involved comparing the DNSPs' total forecast opex with an alternative estimate developed by the AER that reasonably reflects the opex criteria. This alternative value was developed through a combination of outputs from a number of economic benchmarking models and adjustments to account for operating environment factors specific to NSW. The AER then applied a number of category analysis measures to diagnose further areas of potential inefficiency.

To establish an alternative opex, the AER considered a cautious approach to benchmarking was appropriate to mitigate the potential risk of modelling and data error. In combination, the AER

¹ AER, Draft decision, Ausgrid distribution determination 2015-16 to 2018-19 Overview, p. 54; AER Overview, Endeavour, p.53; AER Overview, Essential, pp, 52-53.

reduced the benchmark level of efficiency to approximately 18% less than the frontier predicted by its preferred benchmark model.²

Origin's position

Origin considers that the AER has provided clear evidence for a downward adjustment to each of the DNSPs' base year opex. While the formation of Networks NSW has generated some improvements and efficiencies, these do not fully offset the underlying operational inefficiencies.

Benchmark modelling undertaken by the AER's consultant (Economic Insights) revealed that, in an environment where productivity across the sector is declining, the NSW DNSPs were the least productive in the National Electricity Market (NEM).³

While the AER's preferred benchmark model revealed significant inefficiencies in the DNSPs' base opex, Origin notes that the AER's other four benchmarking models also revealed significant inefficiencies with Ausgrid between 43% and 55% less efficient than the frontier business while Endeavour was between 30% and 41% and Essential between 36% and 52%.

To support its analysis, the AER also undertook partial performance indicators (PPI) of total customer cost and opex per customer. These PPIs provide another perspective on the relative efficiency of the DNSPs and provides a useful cross check of the outcomes from the total factor models.

The AER concluded that on the measure of total customer cost, Ausgrid, Endeavour and Essential all have higher costs relative to the most efficient peer business (Powercor). Consistent with total user cost per customer, Ausgrid, Endeavour, and Essential also appear to have high opex costs per customer relative to Powercor

To understand the source of the DNSPs inefficiencies, the AER undertook a detailed analysis of the information supporting the DNSPs' labour costs.

In its review of the labour and workforce management practices of the NSW DNSPs, the AER's consultant (Deloitte) found that the DNSPs' base year would not likely represent efficient costs. For much of the 2009-14 regulatory period, it appeared likely that the DNSPs' labour costs were impacted by a relatively inflexible workforce with limited ability to innovate or respond to changing circumstances with labour costs entrenched in Enterprise Bargaining Agreements (EBAs).

The AER's body of evidence clearly supports the view that the DNSPs' proposed base year opex is not reflective of the base costs that would be appropriate for the purposes of forecasting expenditure over the 2014-19 period in accordance with the opex criteria.

In adjusting the base opex, Origin agrees with the AER that a holistic approach balances the evidence from multiple lines of analysis. In this regard, Origin supports the AER's decision to recognise general limitations of the benchmarking model with respect to data imperfections and other uncertainties. Notwithstanding, we note that the outputs from the multiple sources have produced consistent conclusions that there are material inefficiencies in the DNSPs. For this reason we consider the AER adjustments result in a balanced decision that reflects both the degree of existing inefficiencies in the DNSPs while at the same time providing an allowance that a prudent operator would require to achieve the operating expenditure objectives.

² The Cobb Douglas stochastic frontier analysis.

³ AER, Electricity distribution network service providers Annual benchmarking report, November 2014, p. 6.

1.3 Step Changes

Background

Step changes allow for adjustments to the efficient base level of opex to account for changed circumstances in the forecast period not otherwise addressed in the DNSPs' opex forecast.

In its submission to the DNSPs regulatory proposal, Origin raised a number of concerns regarding the step change costs put forward by the DNSPs, especially as a result of changes to cost allocation, transitional service agreements and restructure efficiency programs. Origin also considered that the level of detail and presentation of data put forward by the DNSPs was insufficient to support their proposals.

AER's draft decision

The AER's position is that step changes should generally relate to a new obligation or some change in the DNSP's operating environment beyond its control. It is not enough to simply demonstrate an efficient cost will be incurred for an activity that was not previously undertaken. The AER did not accept the vast majority of costs put forward by the DNSPs.

Origin's position

Origin agrees with the AER's position that costs relating to network reform and transitional arrangements are neither a new regulatory obligation nor a capex/opex trade-off. Furthermore, we also agree with the position that the DNSPs' reform programs are only needed because they are not currently operating as efficiently as they could. In this regard, we consider the AER has rightly excluded the proposed step changes put forward by the DNSPs.

With respect to the \$22.1M proposed by Ausgrid for demand management initiatives, Origin supports prudent investment that reduces peak demand where it is clearly demonstrated that the benefits outweigh the costs. However, we agree with the AER's decision to not allow these costs in light of the forthcoming NER changes that will affect how network tariffs are set. Furthermore, on the basis that forecast demand growth for 2015-19 is likely to remain modest, we question the cost benefit tradeoffs of a \$22.1M investment in demand side activities at this point in time.

1.4 Trend

Origin's position

Under the AER's assessment approach, the annual rate of change accounts for changes in real opex taking into account input prices, output growth and opex partial productivity. Based on this definition, Origin supports the AER method to establish a trend that ensures the approach to derive the efficient annual rate of change is consistent with the approach to derive the efficient base.

1.5 Transition to Efficient Opex

Background and AER's draft decision

The DNSPs have acknowledged that current practices and expenditures are inefficient. In response, the DNSPs have demonstrated that they taking steps to address these inefficiencies over time.

The AER is seeking views on whether it is appropriate to allow the NSW DNSPs to transition from their current opex to what the AER has determined as efficient expenditure. In the event that a transition is considered appropriate, the AER has asked how such a transition should be funded.

Origin's position

Consumers have funded the current levels of opex which were approved by the AER as part of its 2009 Determination. These costs are now considered materially inefficient. Origin notes that while the DNSPs have put in place efficiency programs for the 2014-19 regulatory period, these are insufficient to address the inefficiencies identified by the AER.

Origin is strongly opposed to any suggestion that consumers continue to fund the inefficient costs of the DNSPs until they are able to transition to efficient levels.

Origin considers that the recovery of any costs that do not meet the opex criteria set out in the NER must be borne by the DNSPs, not consumers. To the extent that the DNSPs have enjoyed the benefits of excessive opex funding, the onus of responsibility to restore network prices to efficient levels must reside with the businesses, not the consumers.

2 Forecast Capex

2.1 Summary

- Strongly of the view that the onus must be on the businesses to demonstrate that proposed expenditure is underpinned by prudent systems consistent with good operating practice and that these systems are using robust and reliable data. Where this is not made available, Origin considers that the AER's alternative replacement and augmentation programs better reflect the capex criteria set.

2.2 Replacement Capex

Background

Replacement capital expenditure (repex) is non-demand driven capex. It involves replacing an asset with its modern equivalent where the asset has reached the end of its economic life. Economic life takes into account an existing asset's age, condition, risk of failure, technology or operating environment. In general, the AER classifies repex where the expenditure decision is primarily based on the existing asset's inability to maintain efficiently its service performance requirement.

The AER's approach to assessing repex includes comparing data from all NEM DNSPs using the reported expenditure and replacement volume data to derive benchmark unit costs for the standardised network asset categories. As per its Guideline, the AER also derived benchmark replacement lives (the mean and standard deviation of each asset's replacement life) for the standardised network asset categories.

In our response to the DNSPs revenue proposals, we highlighted concerns about the quality and consistency of the information presented by the DNSPs and the difficulty for stakeholders to make informed contributions to the regulatory debate as a result.

AER's draft decision

As raised by Origin previously, and highlighted by the AER and its consultants, the lack of an orderly presentation of information is a contributing factor to the poor governance of capex forecasting. Furthermore, the AER and its consultants have identified systemic failings undermining the prudence of the proposed expenditure, most notably by the lack of robust information and analysis. This has resulted in DNSPs' repex forecast being overstated.

The AER highlighted that the DNSPs methodologies did not have sufficient regard to top-down efficiency tests or delivery strategies. The AER's consultants (EMC^a and WorleyParsons) considered that the DNSPs lack of orderly presentation and disjointed identification of replacement capital expenditure in its budgets and RIN submissions is a contributing factor to the poor governance of their capex forecasting. EMC^a also concluded that Ausgrid's prudence was undermined by a lack of robust information and analysis. This included a conservative operational risk framework that overstated the risk posed by assets, insufficient quality data to make optimal assessments to justify the volume and timing of activity, and failure to provide comprehensive cost-benefit analysis to support some of its key asset strategies.

EMC^a also noted that Ausgrid's risk assessments were subjective and relied upon engineering judgement to assess the acceptability of risk. The consultants observed that Ausgrid used its risk framework results that were not supported by adherence to any particular framework to underpin the recommended replacement strategy. While not to the same extent, EMC^a noted deficiencies in the risk management approaches adopted by Endeavour and Essential. In these instances, the DNSPs systemically overstated costs due to inadequate options analysis and a lack of justification of the timing for resolving the condition-based issues.

Based on the outputs from its various predictive modelling techniques the AER has proposed an alternative repex program that is significantly lower than the programs proposed by the DNSPs.

Origin's position

Origin supports the application of a top down approach to demonstrate that a level of overall restraint has been brought to bear. Using only a bottom-up assessment has a tendency to overstate required allowances as they do not adequately account for inter-relationships and synergies between projects or areas of work which are more readily identified at a portfolio level.

Over the last regulatory period, the DNSPs incurred levels of expenditure well above the historical trend. This was largely driven by higher than expected demand and prescriptive security standards, neither of which remains for this regulatory period. This high expenditure has delivered significant spare capacity in the networks as a result of investments to meet expected demand that did not eventuate. Origin considers that the improvements in network utilisation, coupled with downgraded demand and security of supply requirements, should result in an observable reduction in the amount of required capital expenditure over the 2014-19 regulatory period.

Origin is strongly of the view that the onus must be on the businesses to demonstrate that any revised proposal is underpinned by prudent systems consistent with good operating practice and that these systems are using robust and reliable data. Where this is not made available, Origin considers that based on the information presented that the AER's alternative program better reflects the capex criteria set out in the National Electricity Rules. In that context, the magnitude of the differences between the alternative program and the initial proposals need to be considered in the context of the changed operating environments of the DNSPs as well as the robustness of their planning capabilities.

Notwithstanding, we also note that the DNSPs will be entitled to include prudent capex that exceeds their regulatory allowances into their respective RABs subject to the AER's Capital Expenditure Sharing Scheme.

2.3 Augmentation Capex

Background

Growth driven capex is typically triggered by a need to build or upgrade a network to address changes in demand or to comply with quality, reliability and security of supply requirements. Hence, the main driver of growth-related capex is maximum demand and its effect on network utilisation and reliability.

The main drivers of augmentation capex over the 2009-14 regulatory period were prescriptive security of supply requirements set out in the DNSPs licence conditions and peak load and energy consumption.

As previously noted, prescriptive security of supply requirements have been removed from the DNSPs licence requirements while maximum demand is not expected to reach its previous peak during this regulatory period.

AER's draft decision

The significant investment undertaken over the 2009-14 period has resulted in significant improvement in spare capacity and network utilisation. As a result, the AER's view is that there is some excess capacity in the network that needs to be more efficiently utilised before additional augmentation investment.

The AER engaged WorleyParsons to review whether there are any systematic issues that may result in biases in Ausgrid's augex forecasts. Based on its sample of projects and programs, WorleyParsons observed Ausgrid developed its augex forecast primarily on the licence conditions applying in the 2009-2014 regulatory control period and considered in limited detail the impact of the changes to the licence conditions. For example, WorleyParsons investigated five projects Ausgrid deferred

from the 2009-2014 regulatory control period to the 2014-2019 period. Despite the repeal of the NSW licence condition design standards, WorleyParsons found no evidence Ausgrid used cost optimisation or risk-based techniques in its augex forecast.

In addition, concerns that were identified as part of the DNSPs repex planning were also evident in the augmentation programs. The AER consultants found that the DNSPs (most notably Ausgrid) did not demonstrate evidence of prudent or efficient risk management processes and there is a strong indication that risk-based assessments have not been used in developing forecasts. As a result, the costs proposed by the NSW DNSPs are likely to be higher than would be incurred by a prudent and efficient service provider.

WorleyParsons concluded that Ausgrid's augex costs were likely to be higher because of the use of higher 2013 demand forecast and previous licence conditions as bases for modelling which will bias expenditure forecasts upwards.

Origin's position

It is disappointing that the AER's consultants have found that the DNSPs have applied neither correct operating assumptions nor prudent risk management processes to forecast augmentation costs.

While recognising that the DNSPs have proposed significant reductions to their augmentation expenditure relative to actual expenditure during 2009-14, given the amount that has already been invested and the significant change in operating environment, Origin supports the AER's view that the excess capacity in the network needs to be utilised before supporting further augmentation.

The general decline in asset utilisation between 2006 and 2013 provides an indication of significant excess capacity on Ausgrid's network. Origin has obtained independent advice to assist it to better understand trends in substation loads, current demand forecast and substation asset utilisation for the Ausgrid distribution network.

This independent advice reinforces the AER's position on asset utilisation. Specifically, the advice concluded:

- since 2007 there has been a consistent reduction in peak demand occurring across all of Ausgrid's area for winter;
- since 2007 the summer demand has varied with all time peak occurring in 2010/11;
- the majority of the load duration curves are becoming lower and flatter for winter with trends in summer more varied; and
- peak demand is reducing more rapidly than other points on the load duration curve in winter with trends in summer more varied.

The advice goes on to conclude that given the low risk of failures in zone substations compared with the short duration of peak demands, the prospect of a substation failure occurring at the same time as peak demand is low. This report is available to the AER on a commercial in confidence basis.

Origin notes that Ausgrid has used 2013 load forecast to inform the program of work for its 11kV capacity plan. This program represents a significant component of Ausgrid's total augex. The consequence of using the higher load forecasts are higher expenditure projections compared to using the 2014 updated demand spatial forecasts for each of its major substations. We expect Ausgrid to update its demand forecasts as part of its revised regulatory proposal. However, in the absence of any update, we agree with the AER's approach to apply a ratcheted demand to provide an indication of the potential need for augmentation.

Origin also notes that since lodging the NSW DNSPs proposal, the Australian Energy Market Operator (AEMO) has released the final report from its Value of Customer Reliability (VCR) review. In that report AEMO determined state-based VCR values of 30-40% lower than the rates used by the DNSPs. Origin considers that, where relevant, this updated data needs to be factored into relevant planning processes. Given the timing of the AEMO report, we would expect the DNSP to incorporate these into any proposed capex costs as part of their revised proposals.

Consistent with its views on the DNSPs' proposed replacement capital, Origin considers that the DNSPs are responsible for providing forecast costs that are underpinned by good operating practice. To the extent that they do not, the AER's alternative program represents the most representative alternative that meets the capex criteria as set out in the NER.

2.4 Overheads

Origin's position

Origin has previously raised concerns over the deterioration in the capex overhead rate since 2011-12. In the event that there is a reduction to capital, operating and maintenance programs, there also needs to be a reduction to the quantum of on-costs and overheads to remove potential inefficiencies in support services. In this regard, Origin considers the approach of the AER to reduce overheads to reflect reductions in base opex is appropriate. Furthermore, Origin would expect that over the next regulatory period, given the impetus to move towards efficient costs, that this should also be reflected in an overhead rate consistent with efficient industry benchmarks.

3 WACC

3.1 Summary

- Consider the AER has adopted a balanced and pragmatic approach to WACC that provides certain and predictable outcomes for investors and provides a balance between the views of consumer groups and the DNSPs.
- Consider that the AER has adopted a balanced and pragmatic decision to adopt an equity point estimate of 0.7 on the basis it is a modest step down from previous regulatory determinations, thereby providing a certain and predictable outcome for investors and a balance between the views of consumer groups and the DNSPs.
- Consider that there is no evidence to support the assertion that a transition to a trailing cost of debt approach will not provide the DNSPs with an opportunity to recover at least efficient financing costs.

3.2 Equity Beta

Background

The development of the AER's Rate of Return Guidelines has been subject to robust and extensive consultation and review. This Guideline sets out the methodologies the AER uses in determining a return on equity and a return on debt for in its regulatory determinations.

The NER requires that the return on equity for a regulatory control period must be estimated such that it contributes to the achievement of the allowed rate of return objective. The allowed rate of return objective means the rate of return for a DNSP is to be commensurate with the efficient financing costs of a benchmark efficient entity with a similar degree of risk as that which applies to the DNSP in respect of the provision of standard control services. In estimating the return on equity, regard must be had to the prevailing conditions in the market for equity funds.

AER's draft decision

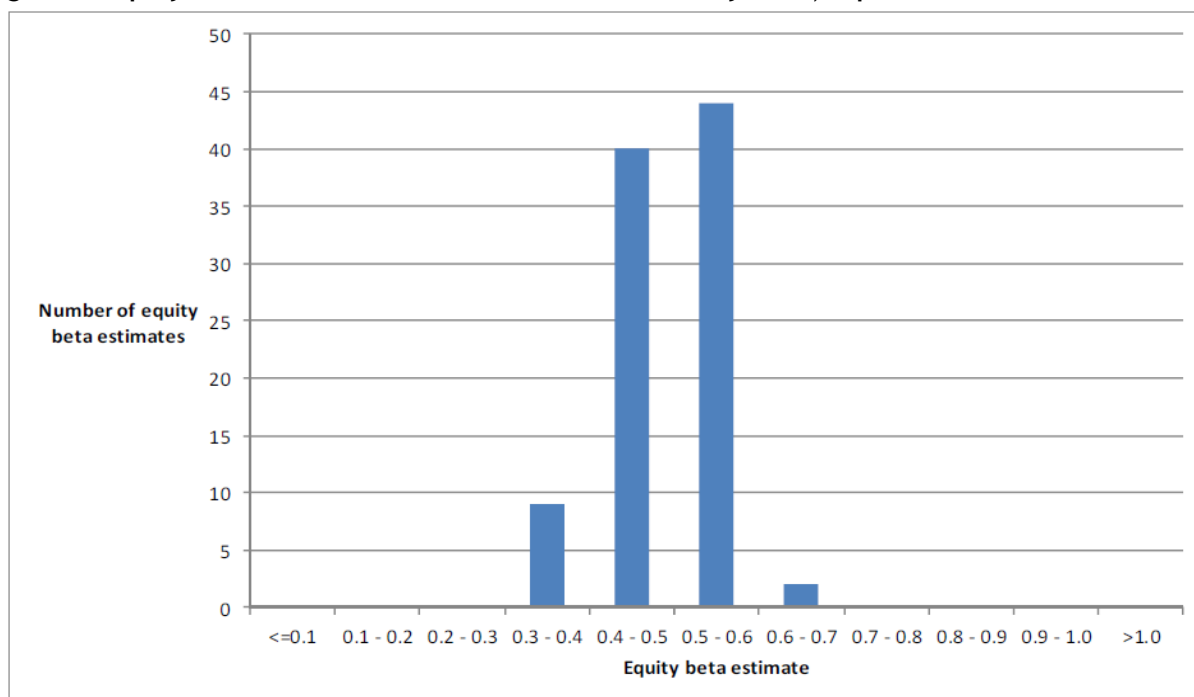
The AER considered that operational risk for the benchmark efficient entity would be above the market average, given the high proportion of fixed costs (relative to variable costs) for energy networks. The AER also considered that intrinsic risk for the benchmark efficient entity would be very low because the DNSPs are insulated from the business cycle largely as a result of a regulatory regime where the businesses are not exposed to volume risk and have a guaranteed revenue stream under the revenue cap arrangements.

As such, the AER did not accept the equity beta of 0.82 proposed by the NSW DNSPs and instead adopted an alternative equity beta point estimate of 0.7.

The AER defined the benchmark efficient entity as a pure play regulated energy network business operating within Australia. To determine systematic risk, it reviewed data for domestic businesses that are considered to be reasonable comparators to the benchmark efficient entity to inform the equity beta estimate.

The AER accepted the equity beta estimates derived by its consultant (Henry). This empirical analysis used a comparator set of nine Australian energy network firms, using available data from 29 May 1992 to 28 June 2013 and showed an extensive pattern of support for an empirical equity beta within a range of 0.3 to 0.8. This distribution is replicated in **Figure 1** below.

Figure 1: Equity beta estimates from AER consultant’s Henry 2014) report



Source: AER Draft Decision, Attachment 3: Rate of Return, p. 258.

The AER considered the equity beta estimates presented by Henry were generally consistent with other empirical studies based on Australian energy network firms. The AER also considered that international comparators were less representative of the benchmark efficient entity and therefore should not be used as the primary determinant of the equity beta range or point estimate.

The AER did, however, consider that the international evidence provides some limited support for an equity beta point estimate towards the upper end of its empirical range.

Origin’s position

Origin considers that for energy network businesses, increases in financial risk as leverage increases is relatively low, largely due to the minimal risks that exist in the current regulatory framework and the ability of the businesses to effectively pass on borrowing costs to consumers.

The AER’s consultants (McKenzie and Partington) noted that given the low default risk in regulated energy network businesses, the financial risk effects are 'unlikely to be substantive in normal market conditions'. McKenzie and Partington concluded:⁴

...it is hard to think of an industry that is more insulated from the business cycle due to inelastic demand and a fixed component to their pricing structure. In this case, one would expect the beta to be among the lowest possible and this conclusion would apply equally irrespective as to whether the benchmark firm is a regulated energy network or a regulated gas transmission pipeline.

The benchmark efficient entity is a pure play regulated energy network business operating within Australia. The regulatory framework which applies to regulated network businesses creates a very low business and financial risk environment that Origin considers is unparalleled. For these reasons, Origin supports the AER’s approach to determine systematic risk based on empirical studies based on Australian energy network firms. Origin also agrees that international comparators should not be

⁴ AER Draft Decision, Attachment 3: Rate of Return, p. 236.

used as primary determinants of risk to the extent that the risks faced by these firms are not directly comparable to Australian conditions.

Origin notes that the data supports an argument for an equity beta lower than the upper range adopted by the AER. However, we consider that the AER has adopted a balanced and pragmatic decision to adopt 0.7 on the basis it is a modest step down from previous regulatory determinations, thereby providing a certain and predictable outcome for investors and a balance between the views of consumer groups and the DNSPs.

3.3 Return on Debt

Background

The NSW DNSPs have proposed a cost of debt of 7.98%. However, the NSW DNSPs have not adopted a transitional approach as set out in the AER's Rate of Return Guidelines. The NSW DNSPs claim that the AER's proposed transition approach would not allow them the opportunity to recover at least their efficient costs of debt finance and have therefore adopted an immediate application of the 10 year trailing average approach.

As set out in its Rate of Return Guidelines, the AER has proposed to estimate the return on debt of the benchmark efficient entity using a trailing average portfolio approach with equal weights applied to all elements of the trailing average and to update the return on debt estimate annually.

The NSW DNSPs stated that they have prudently managed refinancing risks over the past 10 years by issuing debt on a staggered portfolio basis. They have maintained this debt management approach despite the previous cost of debt rule. Therefore, they claim that they do not face the transitional issues of other DNSPs, who were able to finance their total debt portfolios to match the allowed cost of debt under the short term averaging period approach.

Furthermore, the NSW DNSPs claim that given the significant size of their respective debt portfolios and the depth of the interest rate derivative market, there is a real risk that they would not be able to hedge their cost of debt allowance using interest rate swaps. In addition, they argue that even if they were able to: (1) refinance their entire debt portfolio over a short-term averaging period; or (2) use interest rate swaps to match its actual costs to yields observed over a short term averaging period; the pricing of the debt would not be efficient and would come at a significant cost. They therefore argue that a short-term averaging period approach reflects a clearly inefficient approach to managing debt for a benchmark efficient DNSP with a notional debt portfolio of the size of the NSW DNSPs.

Section 7A of the National Electricity Law provide that a service provider should be provided with a reasonable opportunity to recover at least the efficient costs the operator incurs in providing direct control network services and complying with its regulatory obligations.

AER's draft decision

The AER's draft decision is for cost of debt of 6.51%, determined using a 10 year transition to a trailing average benchmark debt rate.

Under the AER's on the day rate, it is expected the DNSPs could manage interest rate risk in a number of ways. These include for example, issuing tranches of debt over the nominated short-term averaging period, by issuing callable debt or using hedging instruments to match a large component of actual interest costs to the allowed cost of debt.

To ensure the changes to the regulatory approach to WACC did not disadvantage DNSPs that have previously entered into long term risk mitigation arrangements, the AER has set out a transitional arrangement. This arrangement helps mitigate any mismatch between the costs allowed and those incurred over the 10 year period following the adoption of the new regime.

Origin's position

The DNSPs agree that the allowed return debt should be estimated using a 10 year trailing average approach. However, they dispute the application of a transition arguing that this approach will under-compensate them to the extent that the spot rates for the cost of debt are below trailing estimates which will prevent them an opportunity to recover efficient costs.

Consequently, the NSW DNSPs proposed an immediate adoption of the AER's 10 year trailing average portfolio approach to the return on debt as they consider this is compliant with an allowed rate of return that achieves the rate of return objective.

As part of its rule determination relating to the economic regulation of network service providers (ERC0134), the Australian Energy Market Commission (AEMC) did not mandate any particular approach to estimating the return on debt. Instead, the final rule sets out at a very broad level the characteristics of three approaches to estimating the return on debt that could reasonably be contemplated by a regulator. The three options are designed to reflect an approach to return on debt based on:⁵

- the prevailing cost of funds approach;
- an historical trailing average approach; or
- some combination of these two approaches.

Furthermore, the AEMC intended the regulator to have the discretion to propose an approach and that this judgement is to be exercised in such a way as to be consistent with the overall allowed rate of return objective.⁶

While the AEMC delegated discretion to the AER in terms of the approach and application of a calculation of cost of debt, it nevertheless considered the issue of transitioning. Specifically, the AEMC engaged SFG Consulting (SFG) to provide advice on a range of matters associated with the regulatory rate of return. With respect to the issue of transitioning, SFG considered that if a material rule change is to be made, it is important to consider an appropriate set of transition arrangements. The lack of any transition arrangements in setting whether the rule change exposes regulated businesses to risks that they did not previously face is likely to be viewed by the market for funds as a signal that a higher degree of regulatory risk should be priced into their provision of funds. Such an outcome is unlikely to be consistent with the national electricity objective (NEO) and revenue and pricing principles (RPP).⁷ SFG went on to state that the type of "rolling in" arrangement that has been proposed by QTC would be an effective means of transitioning from the current Rules to the use of an historical average cost of debt approach.⁸

SFG also noted that if the regulatory allowance was set by not allowing an appropriate transition arrangement, the result would be either a potentially material benefit or loss to the business - and conversely a potentially material loss or benefit for customers. Moreover, an appropriate transition arrangement effectively destroys any incentive or ability for a business to seek to "game" the regulatory allowance by proposing whichever method might result in the highest allowance.⁹

⁵ AEMC, Rule Determination, National Electricity Amendment (Economic Regulation of Network Service Providers) Rule, 2012, p. 90.

⁶ AEMC, Rule Determination, National Electricity Amendment (Economic Regulation of Network Service Providers) Rule, 2012, p. 90.

⁷ SFG Consulting, Rule change proposals relating to the debt component of the regulated rate of return, Report for AEMC, 21 August 2012, p. 46.

⁸ SFG Consulting, Rule change proposals relating to the debt component of the regulated rate of return, Report for AEMC, 21 August 2012, p. 46.

⁹ SFG Consulting, Rule change proposals relating to the debt component of the regulated rate of return, Report for AEMC, 21 August 2012, p. 7.

In terms of addressing the issues of transitioning, AEMC stated that any transitional adjustment required should seek to achieve a neutral financial impact on the affected service provider and consumers.¹⁰

As required under the AEMC's rule determination, the AER developed Rate of Return Guidelines. The development of the Rate of Return Guidelines provided a forum for the merits of different approaches to be examined and rigorously debated by all stakeholders. Origin considers that following consideration of the material presented through this process, the AER has exercised its judgement to arrive at a method to estimate the cost of debt consistent with the AEMC's policy intent.

In terms of what is permitted under the NER, Origin considers there is no impediment that prevents the adoption of a pre-existing approach as part of a transition. The NER provides that if the Guidelines indicate that there may be a change of regulatory approach in future distribution determinations, the Guidelines should also (if practicable) indicate how transitional issues are to be dealt with. We consider that the AER has fulfilled its obligations in this regard.

With respect to whether a transition would prevent the DNSPs from recovering their efficient financing costs, Origin understands that NSW DNSPs secure debt financing through NSW Treasury Corporation. This arrangement provides that NSW Treasury Corporation is the mandated Debt Advisor to the regulated electricity utility sector. For these clients, NSW Treasury Corporation provides advice on liability management strategies, debt benchmarks and market execution strategies, but the clients manage the execution task themselves.¹¹

Despite the fact that the cost of debt of the benchmark efficient entity is based on bond yield data for BBB+ and BBB rated Australian corporate bonds, NSW Treasury Corporation debt issuances reflect the State's AAA credit rating.¹²

To ensure the NSW DNSPs do not receive a competitive advantage as a result of NSW Treasury Corporation's AAA credit rating, the NSW Treasury Government Guarantee Fee Policy for Government Business seeks to ensure competitive neutrality between Government business and the private sector. As a result, a competitive neutrality fee is imposed to ensure neutrality between the allowed regulatory cost of debt and the lower debt issuances that can be obtained from NSW Treasury Corporation.¹³ For regulated utilities, the guarantee fee rate is determined using the debt tenor adopted by the Regulator's debt allowance benchmark tenor.

Therefore, the NSW DNSPs actual cost of debt would appear lower than the efficient benchmark entity cost of debt with any difference captured by the competitive neutrality fee. On that basis, it is not clear to Origin how the NSW DNSPs would be prevented from recovering their actual cost of debt.

The instances of Government owned DNSPs needing to incur competitive neutrality "fees" appear widespread. In the Productivity Commission's (PC) Inquiry into Electricity Network Regulatory Frameworks, it compared the actual borrowing costs of DNSPs with the forecast cost of debt used in the revenue determinations and concluded that the average regulatory cost of debt is 1.25 per cent

¹⁰ AEMC, Rule Determination, National Electricity Amendment (Economic Regulation of Network Service Providers) Rule, 2012, p.68.

¹¹ NSW TCorp, The 32nd Annual Report to Parliament of New South Wales Treasury Corporation For the year ended 30 June 2014, p. 18.

¹² NSW TCorp, The 32nd Annual Report to Parliament of New South Wales Treasury Corporation For the year ended 30 June 2014, p.7

¹³ NSW Treasury, Government Guarantee Fee Policy for Government Businesses, Policy and Guidelines Paper, May 2014.

higher than the estimated borrowing costs.¹⁴ This data is reproduced in **Table 1** below. While there were some limitations regarding the PC's analysis, it highlights the fact that historically regulated DNSPs have not been restricted from recovering their cost of debt under the on the day approach. This is reinforced by the fact that the NSW DNSPs are effectively shielded through their debt arrangements with NSW Treasury Corporation.

Table 1: PC Comparison of the regulatory and actual cost of debt estimates

Network Business	Regulatory cost of debt %	Actual cost of debt %	Difference % points
CitiPower	8.81	8.17	0.64
Powercor	9.35	8.17	1.18
SP AusNet (distribution)	9.19	7.52	1.67
ETSA Utilities	8.87	8.10	0.77
Aurora Energy	8.00	6.50	1.50
Ergon Energy	8.98	7.48	1.50
Energex	8.98	5.94	3.04
Essential Energy (Country Energy)	7.77	7.48	0.29
Ausgrid (EnergyAustralia)	7.77	7.03	0.74
Endeavour Energy (Integral Energy)	7.84	7.55	0.29
Powerlink	8.10	6.98	1.12
SP AusNet (transmission)	8.20	5.99	2.21
Transend	7.79	6.14	1.65
Transgrid	7.78	6.63	1.15

Source: Productivity Commission, p. 208

Furthermore, Origin considers that if a DNSP chooses not to enter into risk mitigation measures that prevent it from achieving the benchmark return, this is through their own choice. It is a fundamental aspect of incentive regulation that firms bear the risk and reward of the choices they make, not consumers. Irrespective of the NSW DNSPs' hedging strategy the task for the AER is to adopt the practices of a benchmark efficient entity.

Origin also considers that it is relevant to consider the incentives that exist for the DNSPs in pursuing immediate application of the trailing average approach. The timing of the switch to a trailing average approach is an important issue because the debt risk premium rise arising from the GFC temporarily boosted the allowed revenues of the business relative to the costs actually incurred. Therefore, there is an incentive for the NSW DNSPs to switch to a trailing average regime so as to lock-in the accumulated GFC benefit before any reversal can take effect.¹⁵

The NSW DNSPs also make the claim that neither they, nor customers, would be adversely affected by immediately moving to a 10 year trailing average approach.¹⁶ On the basis that the NSW DNSPs' approach will increase the WACC relative to what it otherwise would be, there is clear evidence to suggest that customers will be adversely affected through higher charges without any commensurate increase in service.

For these reasons, we consider there is insufficient evidence to support the assertion that a transition to a trailing cost of debt approach is inconsistent with the NER or that it will not provide the NSW DNSPs with an opportunity to recover at least efficient financing. Based on the fact that the NSW DNSPs obtain debt financing through the AAA rated NSW Treasury Corporation, and are

¹⁴ Productivity Commission 2013, Electricity Network Regulatory Frameworks, Report No. 62, p. 207.

¹⁵ M, Lally, The Trailing Average Cost of Debt, Submission to the QCA, p. 35.

¹⁶ Ausgrid Regulatory Proposal, p. 75.

required to pay a guarantee fee, suggest they are already shielded to some degree from risks of non-recovery.

If this is not the case, the onus of proof should be on the NSW DNSPs to provide actual evidence that demonstrates that its debt financing and competitive neutrality balancing arrangements are efficient and result in an outcome where transitional arrangements prevent them from reasonably recovering their actual cost of debt.

If this is not the case, Origin considers that the proposal by the NSW DNSP not to transition simply results in a higher WACC, which is not in the long term interests of NSW electricity consumers.

4 Incentive Mechanisms

4.1 Summary

- Consider that the proposed EBSS rewards are disproportionate compared to the costs faced by consumers to fund the DNSPs' operational inefficiencies over 2009-2014.
- Support the suspension of the EBSS until such time as the DNSPs demonstrate that their opex has achieved efficient levels.
- Consider that it is imperative that the AER ensures that all mechanisms will resume operating in tandem and as intended to ensure the completeness of the regulatory framework.

4.2 EBSS Rewards

Background and AER's draft decision

In Origin's view, a fundamental aspect of an efficiency benefit scheme is that it should not reward lower expenditure from one period only to fund a cost increase in the subsequent period. The objective of the efficiency benefit sharing scheme (EBSS) is to reward the DNSPs for efficiencies on the basis of the difference between actual and forecast opex in that regulatory year less the preceding regulatory year, and to discourage DNSPs from incurring opex in the assumed base year in order to receive a higher opex allowance in the following regulatory period.

As part of their regulatory proposals, Ausgrid and Endeavour have claimed efficiency benefits of \$426.3M and \$195.2M respectively to be added to their regulated revenue in the 2014-19 period arising from the application of the EBSS in the 2009-14 regulatory control period.

Essential Energy on the other hand accrued efficiency losses over the 2009-14 regulatory period.

Origin recognises that the EBSS is designed to reward businesses for becoming more efficient over time. However, the DNSPs (except Essential) are being substantially rewarded for levels of expenditure that have been revealed to be materially inefficient.

Based on Ausgrid's calculations, the EBSS benefits accrued for the difference between its allowed opex and its actual opex for 2012-13 (the base year) is approximately \$100M. When extrapolated over the 2014-19 regulatory period this increases to \$671M of benefits.¹⁷ This is despite the fact that Ausgrid's base opex of \$520.9M compares to the AER efficient base opex of \$314.9M (nominal).

Unlike Ausgrid and Essential, Endeavour does not appear to have provided its EBSS worksheet as part of its regulatory proposal. This has not allowed stakeholders to establish a more informed view on its proposal.

While the AER has made a number of reductions to the proposed claims, most notably to remove provisions for long service leave, annual leave and workers compensation, the majority of EBSS claims are driven by the difference between actual and allowed opex in the base year.

Origin's position

The NER requires that the EBSS must provide for a fair sharing between service providers and network users of opex efficiency gains and efficiency losses. However, notwithstanding that the DNSPs now face substantially lower base opex levels, Origin considers that the rewards for the DNSPs moving from one level of inefficiency to another level of inefficiency over 2009-14 are disproportionate to the costs faced by consumers to fund those inefficiencies.

¹⁷ Ausgrid, Attachment 4.09, Calculation of EBSS carryover for the 2009-14 regulatory period, May 2014.

4.3 Application of the EBSS in Future

Origin's position

Origin supports the suspension of the EBSS until such time as the DNSPs demonstrate that their opex has achieved efficient levels. In our view, to allow the EBSS to operate in its current form would unnecessarily reward the DNSPs for moving from an inefficient base to an efficient base.

However, Origin notes that the regulatory framework consists of multiple mechanisms that interact with one another and are collectively critical to providing incentives and signals post a revenue determination. While Origin supports a short-term suspension of the EBSS, we also consider that it is imperative that the AER ensures that all mechanisms resume operating in tandem and as intended to ensure the completeness of the regulatory framework.

5 Metering Services

5.1 Summary

- Support the decision of the AER to establish an approach to meter charging that removes exit fees thereby promoting competition in unregulated metering services.
- Encourage the AER to re-consider its choice of labour and unit costs within an efficient range to ensure the annual metering charges for existing meters are compatible with encouraging entry into the market for meter provision.
- Consider DNSPs need to provide annual metering charges for new and upgraded meters in a manner directly comparable to the new meter types they are offering.
- Seek clarification on how the price control mechanism operates for the different DNSPs.

5.2 Exit Fees

Background and AER's draft decision

The AER has stated that its intention with respect to metering is to establish a regulatory framework for the 2015-19 regulatory period, which will be robust enough to handle the transition to competition once the AEMC Rule change to expand competition in metering and related services takes effect.¹⁸

A key aspect of the AER's approach is to classify residual metering costs as a standard control service and to recover these costs through network tariffs.

Under this approach, the annual charge for existing customers will include capital cost recovery. The metering charge for a new customer on the other hand will not include a capital cost as they will have made an upfront capital contribution for the installation of an alternative meter. In this instance, the capital cost of the meter will be transferred into the RAB and recovered through network charges. As a result, the customer will not be exposed to a metering exit fee.

Origin's position

Origin supports the decision of the AER to establish an approach to meter charging that removes exit fees thereby promoting competition in unregulated metering services. As noted by the Standing Council on Energy and Resources, competition is also likely to promote innovation that would further reduce metering costs in the long term and increase the range of functions and associated services that can be offered to consumers.¹⁹

Origin also recognises that decisions regarding the commercial governance of contestable metering will be considered as part of the AEMC's Rule change process. An enabler of contestability is ensuring that changes in the treatment of metering costs are reflected in network tariffs in a manner that minimises administrative complexity and avoids unnecessary costs to upgrade the internal and market systems of retailers and future Metering Coordinators.

For this reason, the onus needs to be on the DNSPs to provide retailers with a minimal and simple set of network tariff codes that differentiate regulated and unregulated meter customers to enable simple and least cost integration into retail billing systems.

¹⁸ AER, Draft Decision, endeavour Energy distribution Determination 2015-16 to 2018-19 Attachment 16: Alternative Control Services, November 2014, p. 16-28.

¹⁹ AEMC, Consultation Paper, National Electricity Amendment (Expanding Competition in Metering and Related Services) Rule, 2014, p. 23.

5.3 Annual Metering Fees

AER's draft decision

The AER has accepted the NSW DNSPs' proposed structure for metering charges being an annual metering charge to recover the capital and maintenance costs of the existing metering assets and an upfront capital charge for new or upgraded connections.

The annual metering charge recovers the following specific elements:

- recovery of the residual capital costs of the existing meter;
- maintenance to cover works to inspect, test, maintain, repair and reactive meter replacement;
- reading for the quarterly or other regular reading of Type 5 and 6 meters; and
- meter data services for the collection, processing, storage and delivery of metering data and the management of relevant NMI Standing Data in accordance with the NER.

The upfront capital charge for new or upgraded connections recovers the capital cost of a proactive meter replacement installed by the DNSP at the customer's premises.

While the AER accepted the pricing structure proposed by the DNSPs, it did not accept the input costs used by the DNSPs to derive their charges, The AER developed alternative charges using benchmarking techniques and different input costs.

Alternative annual metering charges approved by the AER for the respective DNSPs are set out in tables 2 to 4. Charges for new or upgraded meters are set out in table 5.

Table 2: Ausgrid Annual Metering Charges as at 2014-15 (\$2014-15)

Tariff Class	Dominant Meter Type	Network Tariff Code ^A	2014-15 Charge	2015-16 Charge
Residential Inclining Block	Type 6	EA010	\$29.38	\$29.60
Residential Time of Use	Type 5	EA025	\$47.62	\$47.86
Controlled Load	Type 5 and 6	EA030, EA040	\$11.96	\$12.08
Small Business Inclining Block	Type 6	EA050	\$40.28	\$40.62
Small Business Time of Use	Type 5	EA225	\$46.36	\$46.60
LV 40-160MWh Time of Use	Type 5 monthly	EA302	\$73.12	\$73.43
Generator Tariff	Type 5	n/a	\$14.15	\$14.28

^A Ausgrid Metering Model, Attachment 8.20

Table 3: Endeavour Annual Metering Charges (\$2014-15)

Tariff Class	Dominant Meter Type	Network Tariff Code	2014-15 Charge	2015-16 Charge
Residential Anytime	Type 6	n/a	\$13.92	\$14.14
Residential TOU -	Type 6	n/a	\$28.34	\$28.58
Residential TOU -	Type 5	n/a	\$114.04	\$114.34
Small Business Anytime	CT	n/a	\$20.17	\$20.40
Small Business TOU -	Type 6	n/a	\$47.08	\$47.37
Small Business TOU -	Type 5	n/a	\$132.78	\$133.12
Controlled Load	Single phase	n/a	\$11.71	\$4.95

Table 4: Essential Annual Metering Charges (\$2014-15)

Tariff Class	Dominant Meter Type	Network Tariff Code	2014-15 Charge	2015-16 Charge
Residential Anytime	Type 6	n/a	\$32.23	\$33.74
Residential TOU	Type 5 & 6	n/a	\$40.75	\$42.22
Small Business Anytime	CT	n/a	\$32.23	\$33.74
Small Business TOU	Type 6	n/a	\$40.75	\$42.22
Controlled Load	Single phase	n/a	\$11.17	\$11.88
Solar (Gross Meter)	Single phase	n/a	\$39.42	\$40.75

Table 5: NSW DNSP New or Upgraded Metering Prices as at 2014-15 (\$2014-15)

Meter Types	Ausgrid	Endeavour	Essential
Single Phase Direct Connected Accumulation Meter	\$43.16	\$41.66	\$29.55
Three Phase Direct Connected Accumulation Meter	\$113.91	\$180.19	\$119.67
Single Phase Direct Connected Interval Meter	\$90.14	\$111.23	\$86.02
Single Phase Dual Element Direct Connected Interval Meter	\$155.11	\$87.86	\$184.50
Three Phase Direct Connected Interval Meter	\$221.12	\$176.37	\$284.54
Three Phase Current Transformer Connected Interval Meter	\$238.50	\$248.18	\$301.51

Origin's position

Arrangements for the competitive provision of metering should be simple and practicable from a consumer perspective. A consumer's decision to take up a new product will be based on the benefits they expect to receive through more customer focussed tariff structures and services.

To achieve this it is necessary that the barriers to competitive investment in metering technology are removed. As previously stated, Origin supports the AER's revised approach to remove the significant barrier of exit fees.

However, another significant obstacle is the transparent unbundling of metering charges from distribution use of system charges, especially for developing the annual meter charge for existing meters. This allows customers to compare the costs and benefits of different metering service options.

To assist in establishing the efficient annual metering charge, the AER requested its consultants (Marsden Jacob) to develop an efficient range of material unit forecasts as well as reviewing labour costs. Marsden Jacob found that the majority of Ausgrid and Endeavour's material unit costs were within the range of current market rates for metering hardware while only some of the costs proposed by Essential were within this range. The range of efficient material unit costs produced by Marsden Jacob compared with the proposed rates of the DNSPs and the rates accepted by the AER are presented in **table 5**.

Table 5: Marsden Jacobs Material Unit Costs (\$2014-15)

Meter Types	Ausgrid	Endeavour	Essential	MJA Range	AER
Single Phase Direct Connected Accumulation Meter- Type 6	\$23.06	\$18.69	22.90	\$18.69 - \$23.00	\$18.69
Single Phase Accumulation Combination Meter	-	\$153.73	-	Insufficient Information	\$153.73
Three Phase Direct Connected Accumulation Meter - Type 6	\$96.09	\$88.51	86.50	\$86.50 - \$100.00	\$86.50
Single Phase Direct Connected Interval Meter - Type 5	\$88.06	\$302.38	63.72	\$63.72 - \$100.00	\$63.72
Single Phase Dual Element Direct Connected Interval Meter - Type 5	\$147.26	\$346.45	149.86	\$126.00 - \$150.00	\$126.00
Three Phase Direct Connected Interval Meter - Type 5	\$202.00	\$421.28	209.84	\$189.27 - \$220.00	\$189.27
Three Phase Current Transformer Connected Interval Meter - Type 5	\$519.00	-	298.78	\$200.00 - \$400.00	\$200.00

The AER adopted material unit rates at the lowest end of the range developed by its consultants. Origin notes that Marsden Jacob used professional judgement to propose a maximum rates for each meter hardware category. This was based on consideration of market data sourced from online advertised prices and through discussions with a number of the major suppliers of type 5 and 6 meters to Australian network businesses.

Origin recognises that the role of the AER is to ensure customers pay only efficient prices. However, the AER's metering decision is made in the context of ongoing policy reform and a key aspect of these reforms is the promotion of competition in metering services.

In setting efficient prices, Origin encourages the AER to consider its choice of labour and unit costs within an efficient range in the context of promoting innovation and competition that would further reduce metering costs in the long term. This would involve taking into account whether the annual metering charges for existing meters are compatible with encouraging entry into the market for meter provision. Setting annual costs at a level below a new entrant's cost of service provision for an interval meter provides little incentive for a new entrant to enter the market and to allow customers to obtain advanced metering infrastructure from a range of competitive providers and therefore benefit from products and services that they could not otherwise access.

Furthermore, Origin considers that there is insufficient transparency in the current unbundled metering costs presented by the DNSPs. The AER has approved annual metering costs for existing assets (tables 2 to 4) and upfront capital costs for new or upgraded meters (table 5). However, it is not apparent what the ongoing maintenance costs associated with new or upgraded meters are.

Essential Energy has provided annual metering charges for customers who pay upfront for their own meter recognising that these customers will only pay for maintenance, reading and data services. These charges are reproduced in table 6. However, it is not clear how these charges map to the new and upgraded meter types set out in table 5. In addition, it is not clear that Ausgrid and Endeavour have proposed annual meter costs for new and upgraded meter types. Origin considers that to provide customers and other stakeholders with a transparent and unambiguous understanding of costs, all DNSPs need to provide annual metering charges for new and upgraded meters in manner directly comparable to the new meter types they are offering.

Furthermore, for the avoidance of doubt, Origin seeks confirmation of any non-capital charges that will be levied by the DNSPs on customers in the event that a customer switches from their existing meter to an unregulated meter provided by a third party meter provider.

Table 6: Essential Annual Metering Charges for New Customers (\$2014-15)

Tariff Class	2015-16 Charge
Anytime Customers	\$14.69
TOU Customers	\$19.71
Controlled Load	\$4.63
Solar Additions (assumes single phase 2 element)	\$19.30

The AER states that its form of price control for metering services is to base the following year's price on the previous year's prices adjusted by CPI and an X factor. With respect to the installation of a new or upgraded meter, the AER has approved an annual schedule of prices for Ausgrid but only a base price for Essential and Endeavour. Origin seeks clarification regarding: (1) how the form of price control applies for Ausgrid given the approval of a schedule; (2) what X factors apply to Essential and Endeavour given only a base price has been approved; and (3) why there is a different approach across the DNSPs.

6 Ancillary Services

6.1 Summary

- Requests that the AER provides a clearer explanation of how it has addressed stakeholder concerns regarding the bundling of de-energisation and re-energisation fees.
- Support the AER decision not to approve the proposed fees for network tariff change requests.
- Request the AER clarifies how and when new services will be integrated into existing business to business systems.

Background and AER's draft decision

The AER has maintained its position from its Framework and Approach decision to apply caps on the prices of individual services in the 2015-19 regulatory control period.

The AER determined that ancillary services would be fee based on the cost of providing the service (labour rates) and the average time taken to perform the services. The resulting fee is fixed and applies irrespective of whether the actual time taken to perform the activity differs from the AER's set benchmark.

However, there are a small number of ancillary services that are to be quoted services. Under these arrangements, the AER approves the labour rates but not the time taken to perform the service.

The AER did not approve the majority of the DNSPs' proposed fees for ancillary network services. It considered that the proposed fees were higher than fees based on maximum benchmark labour rates and for providing ancillary network services.

Origin's position

A number of submissions in response to the DNSPs' proposals identified issues associated with the aggregation of de-energisation and re-energisation fees.

Origin understands that under the DNSPs' proposal the re-energisation and de-energisation activities are combined within the same fee. As a result, if a customer moves out of a premises and a new customer moves in with a different retailer, the charge for the re-energisation is paid for by the customer departing the premises - not the new customer.

A number of submissions highlighted the inequity of this arrangement. However, we do not consider that the AER has provided a sufficiently clear explanation of how it has assessed the concerns raised by stakeholders. We therefore request the AER provides this analysis in its final decision.

Origin also notes that the DNSPs have proposed a number of new services. The majority of these new services do not align with existing business to business service order specifications. We seek clarification from the AER regarding how and when these services will be integrated into existing interface systems in order to avoid unnecessary and inefficient manual processing.

With respect to network tariff change requests, we support the decision of the AER not to approve the proposed fees on the basis that retailers have no visibility as to whether the request is valid as this function resides with the DNSP to make this assessment.