27 March 2015

Mr Chris Pattas
General Manager
Australian Energy Regulator
GPO Box 520
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Email: AERInquiry@aer.gov.au

Dear Mr Pattas

**ALTERNATIVE APPROACH TO RESIDUAL METERING COSTS CONSULTATION PAPER**

Origin Energy (Origin) appreciates the opportunity to comment on the Australian Energy Regulator's consultation paper on an alternative approach to the recovery of the residual metering capital costs through an alternative control services annual charge.

Origin is strongly of the view that the AER's decision with respect to the recovery of metering costs must promote competition in metering services as this is necessary to support interlinked reforms that will allow network prices to reflect the long run cost of supply and support efficient investment. These developments promote the National Electricity Objective and are in the long term interests of electricity consumers.

While we appreciate the AER is working to a tight timetable to finalise its revenue determinations for the New South Wales Distribution Network Service Providers (DNSPs) by April 2015, we are concerned at the lack of supporting analysis and evidence provided in this consultation paper and the very short consultation period (one week) for such an important and material issue. Our response therefore assesses the AER's metering cost recovery options from a principled basis and identifies what additional analysis is necessary to confirm how Option 2, the Origin preferred approach, would operate in practice, not just for one NSW DNSP, but for all NSW businesses and Queensland and South Australian DNSPs also.

Origin is concerned that the AER has indicated a strong preference for Option 1, which would effectively return to the DNSPs' original position of applying metering exit fees, the only difference being that the customer would bear the cost of legacy metering investments for the remaining life of the asset base rather than as a lump sum. This is an outcome the AER rejected in its NSW DNSP draft decisions and should reject again in its final determinations.

**Context**

As part of the Power of Choice Review, the AEMC recommended a competitive approach for investment in metering and data services for the residential and small business consumer sector.[1] A key element of the AEMC's proposal was that meter costs would be unbundled from distribution use of system charges (DUOS) so that consumers could have confidence that going forward they would be paying for their upgraded meter installation and not continuing to pay for the removed, old existing meter.[2]

[1] AEMC, Power of Choice Review Final Report, p. 83.
[2] AEMC, Power of Choice Review, Final report, p. 88.



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To manage their stranded asset risk, the NSW DNSPs proposed the introduction of a metering exit fee. Consistent with the AER's Draft Determination, we are firmly of the view that a meter exit fee would create a significant barrier to the uptake of smart metering technology. This, in turn, would curtail the effectiveness of the network tariff reform process, which is a key enabler of more informed customer network use, lower future network expenditure and therefore network tariffs.

To address the underlying rationale for proposing an exit fee, the AER initially proposed an approach where the residual asset costs would be recovered through standard control service (SCS) charges. At the time, Origin strongly supported this position.

However, ActewAGL has since argued that it is legally impermissible to add the metering residual to the SCS regulatory asset base (RAB) during a regulatory control period. In light of these concerns, the AER is proposing an alternative approach where the residual would be recovered through an unavoidable annual metering charge that applies to all customers until the metering asset base (MAB) is fully depreciated.

**Revised AER Proposal on residual metering cost recovery**

The AER has proposed that the unavoidable charge could be recovered by one of two ways:

1. the whole MAB is recovered through an unavoidable charge (Option 1); or
2. the component of the MAB at risk of stranding (churned assets) is recovered through an unavoidable charge (Option 2).

The AER has not, however, included a level of analysis in its consultation paper that would allow Origin, or any other stakeholder, to make a fully informed decision on the merits of one option over the other.

The structure and quantum of metering charges will have a material impact on the level of competition in metering services. For this reason, extensive analysis must be undertaken to ensure that metering charges are logical and consistent. For example, the AER's draft annual metering charges for Essential Energy ($33.74) and Ausgrid ($29.60) are both double that of the adjacent Endeavour network ($14.14) for the same service. As a result, the value a customer in the Endeavour network places on smart metering technology will be vastly different to a customer in Essential or Ausgrid networks. The practical effect is that this inhibits competitive entry into the market.

The analysis provided by the AER in its Consultation Paper is limited to an illustrative example provided by Ausgrid. As a result, it is not clear how the unavoidable annual charges behave under different churn rates, across different tariff classes and metering configurations, and over time and whether there are potential unintended consequences because future prices are unknown under all conditions. We consider these scenarios should be reasonably capable of being modelled.

Similarly, how the respective unavoidable and avoidable annual charges relate under different churn rates and over time are also unclear; so too are the potential implications for future metering competition.

Based on the two options provided and within the constraint of the limited available analysis, we strongly favour Option 2. Notionally, this option meets the dual objective of avoiding asset stranding while at the same time preserving the intent of the Power of Choice Review to promote competition in metering and data services. We also consider that this option could be further enhanced through a more accelerated depreciation rate than currently exists and for all future replacement expenditure to be treated as opex.

We do not support Option 1. Under Option 1, in the event a customer elects to install a smart meter, they will be required to pay a capital charge on both their new and existing meters. This effectively acts as a barrier to competition in a manner similar to an exit fee. Option 2 overcomes this impediment by removing this double recovery while also allowing the DNSP to recover the costs of its stranded metering assets.

The AER considers Option 1 better addresses inherent cross-subsidies. However, there is insufficient analysis provided in the consultation paper to identify the extent of these cross-subsidies and their values under different churn conditions and over time. Therefore, it is not apparent that the benefit of eliminating this cross-subsidy would outweigh the higher expected benefits of competition and smart meter penetration under Option 2.

In terms of the administrative impacts of the two options, we are of the view that the data collected should be no different between the options on a year on year basis. The incremental administrative effort would be minimal and largely attributable to updating annual prices under Option 2; this should be an automated process. For these reasons, we consider that the selection of one option over the other should not rest upon an assessment of modest administrative costs. The impact of each option on facilitating metering competition should carry greater weight in determining which option delivers price and service outcomes that are in the long term interests of consumers.

While we support Option 2 in principal, the lack of time available as part of this consultation precludes identification and consideration by stakeholders of potential alternative options that may produce more suitable incentives. Notwithstanding, it is critical that the appropriate analysis is undertaken to inform stakeholders fully of how different churn rates, metering configurations and tariff classes impact both the avoidable and unavoidable charges for each option over time. Where this analysis reveals perverse charging outcomes or an impediment to competition for metering services, any constraint in the AER being able to resolve these issues appropriately should be addressed as a matter of priority through the AEMC metering contestability Rule change process before it is finalised.

**Summary**

Option 1 would effectively return to the DNSPs' original position of applying exit fees in full to those customers who migrate to a 'Smart meter'; the only difference is that under Option 1 a customer taking a smart meter will bear the cost of legacy metering investments for the remaining life of the asset base rather than as a lump sum. This is an outcome the AER rejected in its NSW DNSP draft decisions and should reject again in its final determinations.

The AEMC's Power of Choice Review has delivered a set of policy recommendations and Rule changes directed at promoting competition in new metering and data services to improve consumers' understanding of their electricity consumption and what they can do to reduce or change it. The structure and level of metering charges has a direct impact on how effective and timely advanced metering technology can be rolled out into the existing market. Metering technology is also interlinked to network tariff reform, which underpins the achievement of long run efficient investment in the network infrastructure. Indeed, it is now difficult to imagine a future world without home generation, battery technology, electric vehicles and more sophisticated energy management. Yet the efficient adoption and use of these technologies and realisation of consumer benefits will be dependent on a market led deployment of smart meters, which, in turn, will be heavily influenced by the AER's treatment of residual metering costs.

A decision based on fully informed and robust analysis is a materially preferable outcome than the current AER position. For this reason the AER must undertake the necessary analysis. Where it is constrained in making a decision that is in the long term interest of consumers, this impediment should be removed as a matter of priority through the AEMC metering contestability Rule change process before it is finalised.

**Closing**

Origin would be pleased to discuss any matters raised within this response further with the AER. Please contact Sean Greenup in the first instance on (07) 3867 0620.

Yours sincerely

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