

Submission to AER Consultation Paper: Approach to the recovery of the residual metering costs

1. Introduction

The AER released a consultation paper on 20 March on an alternative approach to the recovery of the residual metering capital costs “residual costs” through an alternative control services annual charge. The paper presents two options for dealing with exit fees arising from a concern about the impact of exit fees on the contestable metering market by creating a new Alternative Control Service (ACS) to recover exit fees from all users rather than just users exiting from a type 5 or 6 meter.

QCOSS is concerned that it appears the AER has already made a decision that it is appropriate to allow distributors to recover these residual costs, and that these costs should be smeared across all customers. It appears the question for consultation posed by the AER in this paper is limited to identifying the most appropriate means to do this. However, QCOSS does not consider that Queensland stakeholders have had an adequate opportunity to consider whether or not it is appropriate to recover residual costs. QCOSS is concerned that the AER has released this paper with only one week to provide submissions, even though this issue will affect hundreds of millions of dollars of metering assets. QCOSS is also concerned that the consultation paper was circulated on a limited release, noting the limited number of stakeholders the paper was issued to when compared to the large number of stakeholders that have participated in workshops, submissions, and consultations for the NSW, Qld, and SA electricity determinations.

QCOSS is cognisant that the AER has to make a final decision with respect to the ACT and NSW determination on the issue of the recovery of residual costs by 30 April 2015. However, it is important that the consultation process for the Queensland determination provides an opportunity to consider these matters in relation to the Queensland regulatory proposals. In its Preliminary Determination for Queensland it is expected that the AER will set out its rationale to the recovery of residual costs, how large these costs will be, and how distributors will be incentivised to actively reduce these costs if they are to be borne by consumers. It is at that stage that different options could reasonably be canvassed as to the recovery of residual costs.

QCOSS’s view is that only very limited residual costs should be recovered from consumers as the old meters are not providing a service and therefore it is only appropriate to recover disposal costs associated with obsolete assets. At a minimum, if the AER does propose to allow the distributors to recover remaining capital costs, QCOSS strongly believes distributors must be “incentivised” to reduce the value of these old meters, to seek out cost-effective solutions to their disposal, and not to pass on legacy costs associated with previous investment decisions to consumers. Further, as advanced meters are rolled out there will be cost savings for distributors which should be taken into account by the AER in deciding how much of the residual costs to recover. Arguably there will also be

cost savings to distributors of reduced operating expenditure (opex) which can be offset against any residual costs. Moreover, in our submission to the AER on the Energex and Ergon Energy's Regulatory Proposals, QCOSS recommended that the AER review the methodology and assumptions used by both Queensland Distributors for estimating the opening value of the metering RAB and the RAB for standard control services (SCS), and that the AER provide guidance to the Distributors on how they value their metering RAB to ensure consistent valuation approaches. We would like to reiterate the importance of this again in this submission.

2. Rationale for approach

The options proposed in the Consultation Paper reallocate exit costs from those that create the exit costs (by switching from existing type 5 and 6 meters) to other parties (those who do not switch from type 5 or 6 meters). QCOSS considers that these options argue for a transfer of costs from consumers exiting type 5 or 6 meters to all consumers. This transfer of costs relieves one set of consumers from the costs that they create (exiting consumers) and smears it across all consumers including those who do not or cannot exit. This artificially raises costs on all consumers and artificially reduces costs on exiting consumers. Both options 1 and 2 present different mechanisms for implementing this approach and therefore both approaches entrench a cross-subsidy from all consumers to consumers exiting from type 5 or 6 meters. QCOSS is not in a position to support such an approach and would need to see the cost implications for all consumers.

Equally, QCOSS does not support the charging of relatively large exit fees either. Energex and Ergon propose such fees in their Regulatory Proposals and these are in the order of \$290 to \$324 for Energex and \$137 to \$166 for Ergon. QCOSS agrees with the consultation paper's rationale for the approach underpinning the options, namely that "*a large exit fee would create a barrier to entry into a contestable metering market following the AEMC's rule change*" (Consultation paper, p. 3). The significant size of the exit fees in Queensland (which are larger than those in NSW distributors) would suggest that even if smeared across all consumers the impact would result in significant cost impost.

In principle, QCOSS's view is that it would be inappropriate to recover residual costs associated with a service that customers are not getting any benefit from. This means that distributors should not be allowed to recover such costs from consumers - either through a charge which is allocated across all customers nor via individual exit fees. The Queensland Distributors' meter fleets are large and include a mix of meter types, ages and conditions. Arguably, at least some of the meters are fully depreciated and have been paid for. QCOSS believes distributors should write off some of these meters, especially those with limited remaining economic lives, and take them permanently out of the metering RAB. Ergon for example would appear to be accelerating its depreciation (presumably to avoid stranded metering assets) and is proposing to recover such charges from customers. Such approaches are not appropriate and consumers should not have to bear the full burden of stranded assets against the background of major structural reform for metering services.

If advanced meters are installed in significant numbers over the period 2015-2020 there will be significant benefits to the distributors. These include lower meter reading costs, lower costs of network operation (e.g. faster fault location, smart grid operation), and savings in capex (particularly in conjunction with demand-based network tariffs). These have been evident in New Zealand and in Victoria where a number of cost-benefit analyses of smart meters identify benefits to distributors from smart meter installation. As

raised in our Submission to the AER on the Queensland Regulatory Proposals, QCOSS considers that the AER should take account of these benefits to adjust the distributors' opex and capex programs in line with reasonable assumptions of the roll-out of advanced meters. It is important that the AER investigates this especially as both distributors are assuming they will be installing large numbers of new meters.

QCOSS refers the AER to its submission on the Queensland Distributors' Regulatory Proposals, specifically Section 6.2, Metering Services. In this submission, QCOSS raises a number of questions which we expect the AER will address in its Preliminary Determination for Queensland (due on 30 April 2015). In summary, QCOSS is concerned that differences in methodological approaches and underlying assumptions can result in material differences in the metering capital costs of different distributors. This is evident in the significant differences between Energex and Ergon's value of its metering RAB, depreciation cost, rate of depreciation, and exit fee. It is recognised that there are a number of methodologies which may be validly employed here, however QCOSS believe there is a need for greater transparency, explanation and guidance from the AER around such methodologies. This is particularly important should the AER proposed to allow distributors to recover these residual costs from consumers. As it will be consumers who bear the risk, every effort should be made to ensure that the methodology adopted is one which minimises the cost impact for all customers.

3. Legal consistency of the approach

The AER's approach may not be legal under the NER. The AER's role is to regulate distribution services (NER 6.1.1), which are defined as "[a] service provided by means of, or in connection with, a *distribution system*" (NER 10). It is not clear that either option 1 or 2 are distribution services in this sense. The AER proposes to regulate aspects of metering services as alternative control services. These are defined as a subset of direct control services, which are in turn defined "a direct control network service within the meaning of section 2B of the Law [which is understood to be the *National Electricity (South Australia) Act 1996*"]". Direct control services are not defined in section 2B of the Law but direct control network services are defined. Direct control network services are defined as:

A direct control network service is an electricity network service—

(a) the Rules specify as a service the price for which, or the revenue to be earned from which, must be regulated under a distribution determination or transmission determination; or

(b) if the Rules do not do so, the AER specifies, in a distribution determination or transmission determination, as a service the price for which, or the revenue to be earned from which, must be regulated under the distribution determination or transmission determination.

It is not clear that the proposed ACS service of a smearing of exit costs for type 5 and 6 meters is an *electricity network service* within the meaning of section 2B. At most it would appear to be an aspect of a service and could instead be a financial service. If there is any reasonable doubt that the proposed ACS services are legal, it is critical for the AER to investigate and confirm their legality given the disruption that could be caused by trying at a future date to correct or unpick a legally challengeable approach.

4. Summary

QCOSS has a number of concerns with the AER's Consultation Paper – namely that:

- In principle, only very limited residual costs (associated with disposal) should be recovered from consumers – either in the form of exit fees or smeared across all customers – as metering assets are not providing an economic service;
- There are inconsistencies and a lack of transparency in the valuation and costs associated with metering services as set out in the Queensland Distributors Regulatory Proposals which has not yet been investigated or addressed by the AER (at this stage of the process);
- It is premature to comment specifically on the options canvassed in the Consultation Paper without having consulted on the issue of cost recovery, methodology and how to recover remaining residual costs in its Queensland Preliminary Decision; and
- The AER has not provided sufficient time or consulted widely enough (particularly in Queensland) on whether or not it is appropriate to recover residual costs associated with old meters of customers that have churned.

We look forward to an opportunity to discuss this issue with the AER further in relation to the Queensland Network Determination.

About QCOSS

The Queensland Council of Social Service (QCOSS) is the state-wide peak body for individuals and organisations working in the social and community service sector.

For more than 50 years, QCOSS has been a leading force for social change to build social and economic wellbeing for all. With almost 600 members, QCOSS supports a strong community service sector.

QCOSS, together with our members continues to play a crucial lobbying and advocacy role in a broad number of areas including:

- sector capacity building and support
- homelessness and housing issues
- early intervention and prevention
- cost of living pressures including low income energy concessions and improved consumer protections in the electricity, gas and water markets
- energy efficiency support for culturally and linguistically diverse people
- early childhood support for Aboriginal and Torres Strait Islander and culturally and linguistically diverse peoples.

QCOSS is part of the national network of Councils of Social Service lending support and gaining essential insight to national and other state issues.

QCOSS is supported by the vice-regal patronage of His Excellency the Honourable Paul de Jersey AC, Governor of Queensland.

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