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**By email: vic2026@aer.gov.au**

### **Issues Paper: Victorian electricity distributors' 2026-2031 regulatory proposals – form of control mechanism**

AusNet Services, Jemena Electricity Networks, CitiPower, Powercor and United Energy (**distributors**) welcome the opportunity to respond to the Australian Energy Regulator's (**AER's**) Issues Paper for the Victorian electricity distribution determination for the 2026-2031 regulatory control period dated March 2025 (**Issues Papers**).

The Issues Papers are inviting comment on the form of price control for distribution services classified as standard control services for the 2026-2031 regulatory control period, in circumstances where distributors have forecast an increase in electricity consumption and demand in each of their regulatory proposals (**proposals**) for the next regulatory control period. It is understood the AER is concerned higher forecasts risk potential over-forecasting of consumption and demand.

For the reasons discussed further in the Attachment to this letter, we do not believe the National Electricity Rules (**Rules**) permit a departure from a revenue cap specified in the Framework and Approach Paper (**F&A Paper**) for standard control services (**SCS**), in response to AER concerns with consumption and demand forecasts. The Rules only permit a departure from a revenue cap where there has been a 'material change' in 'circumstances' that justifies that departure, and that no form of control mechanism set out in that F&A Paper should apply to those distribution services. Therefore, to change the form of control mechanism to a price cap, the AER must classify SCS as alternate control services (**ACS**) when making its distribution determinations.

We don't believe the regulatory proposals, including consumption and demand forecasts, represent a 'circumstance' or 'material change' as required by the Rules.

- The term 'circumstance' doesn't refer to matters, such as forecast increase in consumption and demand, that are already subject to AER oversight and decision-making in its distribution determinations. The AER can manage uncertainty in respect of consumption and demand through a pass-through regime should it choose. It is noted that AusNet Services, CitiPower, Powercor and United Energy's proposals already include a pass through mechanisms for managing consumption and demand forecast uncertainty arising from the transition to net-zero.
- Further, the forecast increase in consumption and demand can't represent a 'material change' given the increases have been projected for many years.

Even if the Rules permitted a departure, Part C of Chapter 6 of the Rules would no longer apply to the regulation of those services. The AER would need to consult on the manner of regulation of those services, including any exercise of the AER's discretion to apply elements of Part C to those services, and matters critical to the network tariffs customers would pay under a price cap over the 2026-2031 regulatory control period, which are not presently part of distributor's proposals. This would be time intensive, create significant uncertainty for distributors and customers and not be practical at this late stage of the review process.

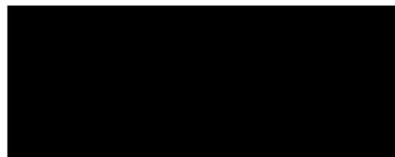
If the AER does depart from a revenue cap, distributors must have the opportunity to reconsider their proposals, including undertaking additional customer engagement which has significantly shaped the development of the current set of proposals developed under a revenue cap. These proposals were predicated on regulation of services in accordance with Part C of Chapter 6 of the Rules. Further, aspects of the regulatory framework are not suited to a price cap. This includes ex-post review provisions in the capital efficiency framework and the tariff structure regime. Interactions between the form of control and these parts of the regulatory framework would need to be carefully considered.

We would welcome further discussion with the AER on the matters presented in this submission. Please contact Renate Vogt with any questions.

Sincerely,



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Regulation  
CitiPower, Powercor, United  
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## Attachment

### The AER Issues Papers

- 1 The Issues Papers identify that the regulatory proposals forecast a significant increase in electricity consumption and demand, and that this increase will occur at a greater rate than in previous regulatory control periods.
- 2 In section 5.1 of the Issues Papers, the AER discusses the forms of control that are to apply to SCS and ACS in the 2026-2031 regulatory control period and, with reference to section 2.2 of the Issues Papers, asks for feedback on the forms of control set out in the F&A Paper. Notably, in the context of discussing the network tariff and bill impacts of the regulatory proposals, section 2.2 of the Issues Papers highlights that, under the revenue cap form of control for SCS in the F&A Paper, the risk of over-forecasting annual energy delivered is borne by consumers, rather than the distributor, which differs from the position under other forms of control, such as a weighted average price cap. The AER also notes, in section 5.3 of the Issues Papers, the role of consumption and demand forecasts in forecasting network expenditure, with the implication being that higher consumption and demand forecasts typically result in higher network expenditure forecasts and, in turn, required revenues.
- 3 By this, the distributors understand the AER to be inviting stakeholders to comment on the suitability of a revenue cap for services classified in the F&A Paper as SCS, in circumstances where the distributors have forecast a significant increase in consumption and demand, and the AER considers this results in the potential for over-forecasting of annual energy delivered.

### The Rules don't permit a departure from the F&A Paper revenue cap form of control for services classified as SCS

- 4 The distributors do not believe their consumption and demand forecasts justify a departure from the revenue cap form of control in the F&A Paper for distribution services classified as SCS.
- 5 As the AER acknowledges in its Issues Papers, clause 6.12.3 of the Rules provides that, in making each distribution determinations, the AER can't depart from the form of a control mechanism specified in the F&A Paper for a distribution service unless:<sup>1</sup>
  - 5.1 it departs from the classification of that distribution service in the F&A Paper, which it is only permitted to do where the AER considers a material change in circumstances justifies the departure; and
  - 5.2 it considers that no form of control mechanism set out in that F&A Paper should apply to that distribution service.
- 6 Therefore to change the form of the control mechanism in the F&A Paper for distribution services classified as SCS, the AER would need to decide to classify those services as ACS (being the only other service classification that would entitle the AER to regulate those services) in making the distribution determinations for the Victorian distributors for the 2026-2031 regulatory control period.
- 7 The Rules limit changes to the form of the control mechanisms in the F&A Paper that the AER may make. The Rules do not permit the making of a change to the service classification in the F&A Paper for the purpose of effecting a change to the form of control. Until recently, in making a distribution determination, the AER had *no* ability to depart from the form of control mechanisms provided for in an F&A Paper. In late 2017, the Australian Energy Market Commission (AEMC) made the Rule change to 6.12.3(c) that conferred the current, limited discretion to depart from the form of control for a distribution service in the F&A Paper, where the form of control for the service in the F&A Paper

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<sup>1</sup> National Electricity Rules, clause 6.12.3(b), (c) and (c1).

would otherwise frustrate the AER's ability to revisit the service classification for the service in that Paper in accordance with clause 6.12.3(b) of the Rules. The AEMC relevantly observed:<sup>2</sup>

*As a change of service classification will most likely necessitate a change in the form of control mechanism, the current clause will significantly limit the effectiveness of the Commission's decision to lower the threshold that applies to the AER's ability to change its service classification between the F & A paper stage and the final determination.*

*The final rule therefore amends clause 6.12.3(c) to allow the AER to change the form of control mechanism for a service between the F & A paper stage and the final determination if it is as a result of a change in service classification made in accordance with clause 6.12.3(b). The AER is still required to maintain the form of control mechanism as set out in the F & A paper in all other circumstances.*

- 8 Clause 6.12.3(b) of the Rules confers only limited discretion to depart from the classification of a distribution service in the F&A Paper, namely in response to a material change in circumstances that justifies that departure.
- 9 The distributors don't consider the forecast increase in consumption and demand in their regulatory proposals to be a 'circumstance' nor a 'material change' for the purpose of the Rules discretion to depart from the service classification in the F&A Paper.
- 10 The distributors don't believe the forecast increase in consumption and demand included in their regulatory proposals to be an over-forecast, a 'circumstance' of the kind referred to in clause 6.12.3(b). The term 'circumstance', in the distributors' view, refers to matters that are the subject of AER oversight and decision-making in its distribution determinations. It is open to the AER to manage any forecasting uncertainty through the use of the pass-through regime, noting that AusNet Services, CitiPower, Powercor and United Energy's regulatory proposals already include a mechanism for managing consumption and demand forecast uncertainty arising from the transition to net-zero.
- 11 Even if we are wrong in this, we don't consider there has been a 'material change' in circumstances, as required to allow the discretion under clause 6.12.3(b) to change the service classification in the F&A Paper. Whilst there are forecast increases in consumption and demand across the 2026-2031 regulatory control period, neither the expected increase nor any of the drivers of that increase have changed in the months since publication of the F&A Paper by the AER in July 2024 – managing this uncertainty was been a key theme of stakeholder discussions preceding the F&A Paper, and the increase and its drivers have been known and anticipated for some time.<sup>3</sup>

#### **A decision to depart from the F&A Paper revenue cap form of control for services classified as SCS is likely an improper exercise of power**

- 12 If the AER were to decide to depart from the revenue cap form of control in the F&A Paper for services classified as SCS, the decision is likely to be an improper exercise of one or both of the Rules powers that would be exercised in the making of that decision.
- 13 Even if the forecast increase in consumption and demand forecasts (or one of the drivers of that increase), or any resultant potential for over-forecasting, were to amount to a 'material change in circumstances' within the meaning of clause 6.2.3(b) of the Rules, the we consider that any decision by the AER that this justifies a change in the classification of those distribution services classified as SCS in the F&A Paper (i.e. to ACS) is likely to constitute an improper exercise of power. A decision that such a

<sup>2</sup> AEMC, Rule Determination, *National Electricity Amendment (Contestability of energy services) Rule 2017*, 12 December 2017 at 101.

<sup>3</sup> See e.g. AEMO publications since 2017: AEMO, *2017 Electricity Forecasting Insights*, Summary Forecasts: Annual consumption overview, available at <[AEMO | Annual consumption overview](#)>; AEMO, Victorian Annual Planning Report October 2023, available at <[2023-victorian-annual-planning-report.pdf](#)> at 3; AEMO, Draft 2024 Integrated System Plan for the National Electricity market, available at <[draft-2024-isp.pdf](#)> at 25-28.

material change in circumstances justifies this change in service classification is only likely to be a proper exercise of the power conferred by clause 6.2.3(b) where the decision:

- 13.1 is reasonable, having regard to each of the mandatory considerations that govern the classification of direct control services as SCS or ACS set out in clause 6.2.2(c) of the Rules and no irrelevant considerations; and
- 13.2 is not made for a purpose other than that for which the clause 6.2.3(b) discretion was conferred.
- 14 We consider that neither the forecast increases in electricity consumption and demand (or any of the drivers of that forecast increase), nor any resultant potential for over-forecasting, engage any of the mandatory considerations that govern the classification of direct control services. To the contrary, each of these mandatory considerations weighs against the making of a change in the service classification of distribution services classified as SCS in the F&A Paper in accordance with clause 6.2.3(b).
- 15 Further, a decision by the AER that the forecast increase in consumption and demand (or any driver thereof), or any resultant potential for over-forecasting, justifies a change in the classification of those distribution services classified as SCS in the F&A Paper would likely be for a purpose other than that for which the clause 6.2.3(b) discretion is conferred. Until 2018, the bar for a departure from the service classification in a relevant F&A Paper was 'unforeseen circumstances'. The AEMC's intent, in lowering the bar to 'a material change in circumstances', was to provide the AER with the ability to respond to changes in technology. The AEMC observed:<sup>4</sup>

*The Commission considers that it is foreseeable that technologies could change between the F & A stage of service classification and the stage where distribution determinations are determined, and therefore lead to a need to reassess a service classification. This has happened in the past, for example, in relation to metering services in several distribution determinations in 2015 due to new rules facilitating the roll-out of advanced meters.*

- 16 We do not see a parallel between the emergence of new technology, and state-wide forecast increases in electricity consumption and demand forecasts (or the drivers of those forecast increases). Applying clause 6.12.3(b) of the Rules to change the F&A Paper classification of distribution services as SCS, in order to effect a change to the revenue cap form of control for SCS in that Paper in the forecast increase in electricity consumption and demand would be inconsistent with the AEMC's statutory intent for the conferral of the discretion to change a Framework and Approach paper service classification (being to respond to the emergence of new technology).
- 17 This is illustrated by the AER's current Distribution Service Classification Guidelines (**Guidelines**). In explaining how the AER interprets the mandatory considerations that govern the classification of direct control services, the Guidelines provide that common distribution services are to be classified as SCS because:
- 17.1 all customers benefit from the common distribution service;
- 17.2 the classification is administratively efficient, and consistent with previous regulatory approaches for many distributor services; and
- 17.3 the classification promotes a consistent regulatory approach to similar services within and across jurisdictions.

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<sup>4</sup> AEMC, Rule Determination, *National Electricity Amendment (Contestability of energy services) Rule 2017*, 12 December 2017 at 100.

- 18 We don't consider that the forecast increases in electricity consumption and demand have any bearing on any of these considerations. While the Guidelines are not binding on the AER in deciding on service classification, the Rules require the AER to explain any departure from the Guidelines in making such a decision. We anticipate this may prove difficult where the AER changes the classification of distribution services classified as SCS in the F&A Paper (i.e. to ACS), to effect a change to the revenue cap form of control for those services in response to the forecast increases in consumption and demand.
- 19 Even if the AER were to decide to change the classification of the distribution services classified as SCS in the F&A Paper (i.e. to ACS) in its distribution determinations, and that decision were a proper exercise of the power conferred by clause 6.2.3(b), a decision to change the revenue cap form of control specified in the F&A Paper for those services is nonetheless likely to be an improper exercise of the power conferred by clause 6.12.3(c) of the Rules.
- 20 The Rules prescribe mandatory considerations to which regard must be had in determining the form of control for ACS, which are set out in clause 6.2.5(d) of the Rules. These include the potential for the development of competition in the relevant market and how the control mechanism might influence that potential, the regulatory arrangements applicable to the relevant services immediately before the commencement of those distribution determinations, and the desirability of consistency between regulatory arrangements for similar services (both within and beyond the relevant jurisdiction).
- 21 Each of the mandatory considerations governing decision-making on the form of control for ACS would weigh against a change in the form of control applicable to the distribution services classified as SCS in the F&A Paper, in response to the forecast increases in consumption and demand. None of these mandatory considerations is engaged by these forecast increases, given that the contestability of provision of, and the form of control adopted previously and in other jurisdictions for, the relevant distribution services would be unchanged. Further, as already discussed above, clause 6.12.3(c) confers a limited discretion to depart from the form of control for a distribution service in the F&A Paper, so as to ensure that the form of control for the service in the F&A Paper would not frustrate the AER's ability to revisit the service classification for the service in that Paper in accordance with clause 6.12.3(b) of the Rules. A decision to change the form of control in the F&A Paper for several distribution services, where the change to the F&A Paper service classification that empowers this is made in pursuance of that change to the form of control, is not a decision made for the purpose for which the clause 6.2.3(c) discretion was conferred.

**A decision to depart from the F&A Paper revenue cap form of control for services classified as SCS would render application of Part C of Chapter 6 to those services discretionary**

- 22 As discussed above, any decision to depart from the revenue cap form of control in the F&A Paper for services classified as SCS in that Paper would necessarily involve the classification of those services as ACS in the distribution determinations.
- 23 Part C of Chapter 6 of the Rules does not apply to ACS. Rather, Part C sets out the building block approach to the regulation of distribution services classified as SCS, and clause 6.2.6 provides that the control mechanism may (but need not) utilise elements of Part C (with or without modification).
- 24 Accordingly, if the AER were to classify distribution services stated to be SCS in the F&A Paper as ACS in its distribution determinations, so as to effect a change to the revenue cap form of control specified in that Paper for those services, it would not be legally required to apply the regulatory approach outlined in Part C of Chapter 6 to those services in making that determination. The application of each of the elements of Part C to those services would instead be a matter within the AER's discretion, and on which it would need to decide in accordance with law.
- 25 The application of all elements of Part C to services that are classified as ACS in the distribution determinations as a consequence of a departure from the SCS classification and revenue cap form of

control in the F&A Paper would call into question whether the making of the decision to depart from the F&A Paper service classification and revenue cap form of control for SCS involved an improper exercise of a power conferred by clause 6.12.3 of the Rules.

**We expect the opportunity to be heard on departure from the F&A Paper revenue cap form of control for services classified as SCS in that Paper**

- 26 If, notwithstanding the matters discussed above, the AER were to consider making a decision to depart from the revenue cap form of control specified in the F&A Paper for the distribution services classified as SCS in that Paper, we would expect to be afforded the opportunity to not only be heard on the proposed decision, but also revisit our regulatory proposals.
- 27 We have submitted regulatory proposals that were premised on the classification of the common distribution services as SCS, and the form of control for these services being a revenue cap, consistent with what is provided for in the F&A Paper, the AER's Guidelines and long-standing regulatory practice. A change from a revenue cap form of control to a price cap form of control for common distribution services constitutes a fundamental change in the regulatory treatment of those services, as would classifying common distribution services as ACS, to facilitate the adoption of a price cap form of control for those services. As discussed above, Part C of Chapter 6 of the Rules would not automatically apply to govern the regulation of common distribution services if they were to be classified as ACS.
- 28 As a revenue cap form of control for the services classified in the F&A Paper as SCS was contemplated in that Paper, our regulatory proposals omit information and forecasts critical for the application of a price cap form of control to those services and, consequently, stakeholders have not had any opportunity to comment. For example, if a price cap form of control were specified in the F&A Paper, we would have been required to input forecast tariff quantities into the post-tax revenue model for each year of the 2026-2031 regulatory control period. As those forecasts are critical to the network tariffs customers would pay under a price cap, they must be robust and subject to stakeholder scrutiny. Given our regulatory proposals were premised on a revenue cap applying to the services classified as SCS in the F&A Paper, these forecasts were not included.
- 29 We, and other stakeholders, would be denied the opportunity to be heard on the regulatory approach for services for which a change to an ACS classification is made, and the other implications of applying a price cap form of control, which is contemplated by the National Electricity Law and the Rules, unless we are provided the opportunity to revisit our regulatory proposals so as to provide, in those proposals, for the potential scenario in which:
- 29.1 the AER decides to depart from the revenue cap form of control specified in the F&A Paper for the distribution services classified as SCS in that Paper, by classifying those services as ACS, in its distribution determinations; and
- 29.2 accordingly, the application of each element of Part C of Chapter 6 to those services is discretionary, rather than mandatory, and a price cap is applied, instead of a revenue cap.
- 30 We consider a decision to change the classification of common distribution services to ACS, to change the form of control applicable to those services, would give rise to significant natural justice and procedural fairness issues, unless we first receive:
- 30.1 a reasonable opportunity to prepare, in substance, an alternative proposal for the relevant services for the scenario in which a change is made to the F&A Paper service classification and form of control, and Part C of Chapter 6 of the Rules is therefore inapplicable to the relevant services;
- 30.2 a draft determination from the AER in response to that alternative proposal; and

30.3 an opportunity to prepare a revised alternative proposal for the relevant services in response to that draft.