



Power and Water Corporation Cost Allocation Method

January 2018

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Shortened forms

Table text heading

AER	Australian Energy Regulator
CAM	Cost Allocation Method
Distributor, DNSP	Distribution Network Service Provider
NEL	National Electricity (Northern Territory) Law
NEM	National Electricity Market
Rules, NER	National Electricity Rules (Northern Territory)
guidelines	Distribution Cost Allocation Guidelines

1 Introduction

1.1 Summary

On 24 November 2017 Power and Water Corporation submitted a Cost Allocation Method (CAM) to the AER for approval — see Appendix A to this paper. Power and Water Corporation is a state owned corporation of the Northern Territory (NT) Government, providing electricity distribution services in the Northern Territory. A CAM is used to separately account for the costs of providing electricity distribution services, including from other services the distributor might provide. Power and Water Corporation has proposed its CAM take effect from 1 July 2019.

We have determined Power and Water Corporation's proposed CAM:

- accords with the requirements of the National Electricity (NT) Law (NEL) and National Electricity Rules (NT) (the rules)
- gives effect to and is consistent with our Distribution Cost Allocation Guidelines (our guidelines).

Accordingly, we have approved Power and Water Corporation's proposed CAM under clause 6.15.4(c) of the rules.

1.2 Background

The AER is responsible for regulating revenues of the electricity distribution businesses in the Northern Territory in accordance with the NEL and the rules. Chapter 6 of the rules provides further details on the economic regulation of electricity distribution services in the Northern Territory.

Cost allocation concerns attributing a regulated business' costs, or allocating shared costs, between distribution service categories and non-regulated business sections. The different services provided by DNSPs are defined in the NEL and the rules. They are:

- direct control services, comprising:
 - standard control services
 - alternative control services
- negotiated distribution services
- unclassified, or unregulated, services.

In our distribution determinations we classify distributor services to the above categories based on factors specified by the rules. The prices DNSPs charge for the different categories of distribution services depend on the costs incurred in providing those services. It is therefore important that cost allocation between service classifications accurately and fairly represents costs incurred in providing those services. We rely upon historical and forecast costs allocated in accordance with an approved CAM to determine prices charged, or revenues raised, by distributors such as Power and Water Corporation.

Distribution regulatory proposals, or the regulatory arrangements proposed by DNSPs to us for a particular regulatory control period, must comply with an approved CAM. The CAM subject to this decision paper will be used by Power and Water Corporation to develop its distribution regulatory proposals. Power and Water Corporation will also use its CAM to report to us annually for its regulated distribution business.

Following our approval, Power and Water Corporation's approved CAM will remain relevant to its regulatory accounts, reporting and regulatory proposals until we approve a further CAM variation.

2 Rule requirements and assessment

2.1 The rule requirements

For DNSPs:

- Clause 6.15.4(a) of the rules requires a DNSP to submit to us for approval a document setting out its proposed CAM.
- Clause 6.15.4(b) requires that a CAM give effect to and be consistent with our distribution guidelines.
- Clause 6.15.4(c) provides for us to approve or refuse to approve a CAM submitted under paragraph (a).
- Clause 6.15.4(f) provides for a DNSP to amend its CAM from time to time, subject to our approval.

2.2 Assessment process

Power and Water Corporation informally submitted a pre-draft copy of its proposed CAM on 13 June 2017. Upon preliminary assessment, we recommended PWC address a small number of minor issues. We also expressed concern that PWC's internal record keeping system does not appear to align with our service classifications and the broader regulatory framework. PWC has indicated to us that it is planning to revise its record keeping system to better match our service classifications. Overall, Power and Water Corporation was provided with feedback that limited corrections were required to permit approval of the CAM.

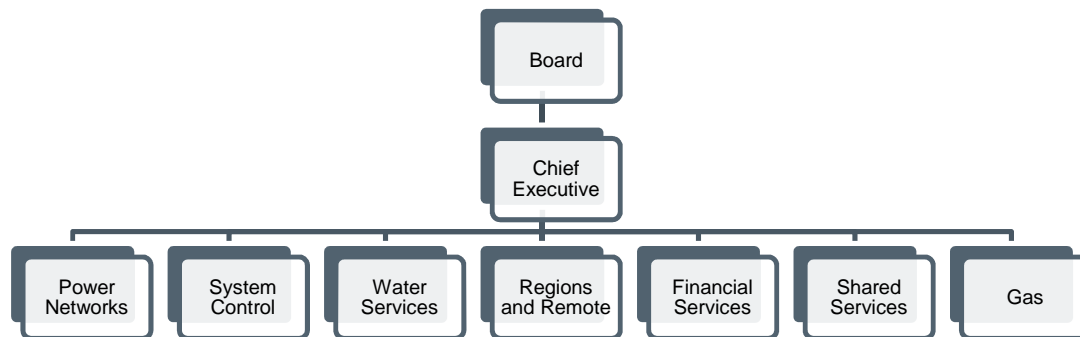
As a result of our feedback on the informal iteration of its CAM, Power and Water Corporation formally submitted a revised iteration of the CAM for our approval. Appendix 2 of the CAM provides a detailed compliance matrix against the requirements of our guidelines and the rules.

2.3 Power and Water Corporation CAM proposal and structure

Power and Water Corporation sought AER approval of the attached CAM under clause 6.15.4 (c) and (d) of the rules. The CAM provides details on corporate structure, attribution of direct costs, allocation of indirect costs, cost recording and record keeping systems, compliance and capitalisation policies.

Power and Water Corporation's proposed CAM describes its corporate structure. In addition to being a distribution network service provider, Power and Water Corporation provides water supply services, sewage services and remote community support services to customers in Northern Territory. The CAM specifies that administrative support functions, billing and call centre functions are shared services amongst the range of services that Power and Water Corporation provides.

Figure 1 Power and Water Corporation corporate structure¹



PWC proposes that

- Indirect costs shall be allocated between its service categories in the same proportion as directly attributed costs.
- PWC's capitalisation policy is consistent with regulatory requirements to ensure the portion of overheads capitalised in the construction of assets is reasonable.
- The allocation of capital expenditure for assets shared amongst service categories will be based on their proportional use as per our service classifications.
- Internal reviews and internal/external audits are part of PWC's monitoring of its own compliance with its CAM.
- Prior to the commencement date of 1 July 2019, PWC intends to use the CAM to compile data for regulatory information instruments and to submit its regulatory proposal for the 2019-2023 control period.

Currently, PWC utilises "work orders" and "projects to record costs in their AMS (Asset Management Systems) and FMS (Financial Management Systems). The costs are entered in the systems based on location and not based on service category (regulated or unregulated). PWC's Chief Executive (Acting) has committed to upgrading PWC's internal accounting system, by no later than 1 July 2020, to ensure it is able to accurately track costs incurred in providing regulated compared to unregulated services.

¹ Power and Water Corporation CAM, p. 10

We note that PWC's non-distribution services are other regulated utility services (water, sewerage) or community support services which are fully funded by Northern Territory Government.

3 Consistency with our cost allocation guidelines

This section sets out our assessment of PWC's proposed CAM against the requirements of our guidelines.

3.1 Power and Water Corporation's CAM assessment

The format and content of Power and Water Corporation's CAM are regulated by clause 3.2(a) of our guidelines. Table 1 compares Power and Water Corporation's proposed CAM against the requirements of clause 3.2(a).

Table 1 CAM assessment table

General obligations

Rules	CAG	Requirements	Addressed
6.15.4(a)	1.5, 3.1(a)	DNSP must develop a proposed CAM for submission to the AER	Appendix A
6.15.4(b)	1.5, 3.1(b)	DNSP's proposed CAM must give effect to and be consistent with the CAG	Appendix A
	5.4	DNSP must maintain current copy of approved CAM on its website	Appendix A - Version history and date of issue

Contents of Cost Allocation Method

CAG	Requirements	Addressed
3.2(a)(1)	Version number	Appendix A -Version history and date of issue
3.2(a)(2)	DNSP's commitment to history and date of issue	Appendix A -Cover page
3.2(a)(3)	Statement of nature, scope and purpose of document and way it is to be used	Appendix A - Section 3.2
3.2(a)(3)A	Accountabilities for implementation	Appendix A - Section 3.3
3.2(a)(3)B	Responsibilities for updating, maintaining and applying document and for internally monitoring and reporting its application	Appendix A - Section 3.4
3.2(a)(4)	Description of corporate and operational structure	Appendix A - Section 4

CAG	Requirements	Addressed
3.2(a)(5)	Specification of service categories and types of persons to whom services provided	Appendix A - Section 5
3.2(a)(6)	Principles and policies for attributing costs to, and allocating costs between, categories of distribution services in accordance with clause 2.2 of CAG	Refer to separate table below
3.2(a)(7)	Description of how will maintain records of attribution and allocation	Appendix A - Section 10
3.2(a)(8)	Description of how will monitor compliance with CAM and Guidelines	Appendix A - Section 11
3.2(a)(9)	Commencement date	Appendix A - Section 12

Cost allocation principles and policies

Rules	RFG	CAG	Requirements	Addressed
6.15.2(1)	3.2.2(a)	2.2.1(a)	<p>Include sufficiently detailed principles and policies for attributing costs to, and allocating costs between, categories of distribution services to enable:</p> <ul style="list-style-type: none"> AER to replicate reported outcomes DNSP to demonstrate that it is meeting requirements 	Sections 8 and 9 and Appendix 1 of Appendix A
		2.2.1(b)(1)	Include specified information on directly attributable costs to enable AER to replicate reported outcomes	Appendix A - Sections 7 and 8
		2.2.1(b)(2)	Include specified information on shared costs to enable AER to replicate reported outcomes	Sections 7 and 9 and Appendix 1 of Appendix A
6.15.2(2)		2.2.2	Attribute costs directly to, or allocated costs between, categories of distribution services based on substance of underlying transaction or event not legal form	Sections 6, 7, 8 and 9 and Appendix 1 of Appendix A
6.15.2(3)(i)		2.2.3	Only directly attribute costs to categories of distribution services if they are directly attributable to the provision of the service	Sections 6, 7 and 8 of Appendix A

Rules	RFG	CAG	Requirements	Addressed
6.15.2(3)(ii)		2.2.4	<p>Allocate shared costs between categories of distribution services using an appropriate causal allocator, except to the extent that:</p> <ul style="list-style-type: none"> • Shared cost is immaterial • Causal relationship cannot be established without undue cost or effort <p>in which case may use non-causal allocator in specified circumstances</p>	Sections 6, 7 and 9 and Appendix 1
6.15.2(4)			Clearly describe the cost allocation method, the reason for using it and the numeric quantity (if any) of the chosen allocator	Sections 6 and 9 and Appendix 1
6.15.2(5)		2.2.5	Do not allocate the same cost more than once	Sections 6 and 9
6.15.2(6)		2.2.6	Detailed principles, policies and approach used to attribute costs directly to, or allocated costs between, categories of distribution services must be consistent with the Distribution Ring Fencing Guidelines	Sections 6 and 9 and Appendix 1
6.15.2(7)		2.2.7	Costs that have been attributed or allocated costs to distribution services must not be reattributed or reallocated to another service during the regulatory control period	Sections 6, 7, 8 and 9 and Appendix 1

4 Decisions

We consider the CAM proposed by PWC gives effect to and is consistent with our guidelines and the rules. We therefore approve, under clause 6.15.4(c) of the rules, PWC's proposed CAM.

Appendix A: Power and Water Corporation's CAM

PWC's CAM is attached as a separate document. Digital copies are available at www.aer.gov.au.