



Endeavour Energy Cost Allocation Method

March 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 21 February 2018 Endeavour Energy submitted amendments to its approved Cost Allocation Method (CAM) to the AER for approval — see Appendix A to this paper. Endeavour Energy provides electricity distribution services in New South Wales. A CAM is used to separately account for the costs of providing electricity distribution services, from other services the distributor might provide. Endeavour Energy has proposed its CAM amendments take effect from 1 July 2018.

We have determined Endeavour Energy’s proposed amended CAM:

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

Accordingly, we have approved Endeavour Energy’s proposed amended CAM under clause 6.15.4(c) of the rules.

1.2 Background

The AER is responsible for regulating revenues of an electricity distribution business in New South Wales 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 New South Wales.

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 Distribution Network Service Providers (DNSPs) are defined in the NEL and the rules. They are:

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

A further category of services is identifiable—non—distribution services. We do not, nor are we able to, regulate these services.

In our distribution determinations we classify distribution 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 Endeavour Energy.

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 amended CAM subject to this decision paper will be used by Endeavour Energy to develop its distribution regulatory proposals. Endeavour Energy will also use its CAM to report to us annually for its regulated distribution business.

Following our approval, Endeavour Energy's approved amended 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

Endeavour Energy submitted informal (draft) copies of the amended CAM to the AER, reflecting changes in organisational structure and changes in allocation of overhead costs. We engaged with Endeavour Energy through various stages of assessment providing feedback on the CAM structure, content and overall presentation. During the assessment process we advised Endeavour Energy to provide details on treatment of depot costs, and their allocation to service categories, in the amended CAM.

Endeavour Energy modified the CAM based on our feedback and formally submitted an amended 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 Endeavour Energy CAM proposal and structure

Endeavour Energy 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 and indirect costs, cost recording and record keeping systems.

Endeavour Energy proposed to amend its existing approved CAM primarily to reflect variations in the allocation of overhead costs. The amended CAM provides a table of allocators used for various opex and capex cost categories. These cost categories closely reflect the cost centres used in Endeavour Energy's internal cost recording systems. In addition, the amended CAM also reflects modifications on corporate structure and allocation of depot costs.

Our guidelines require the CAM to enable the AER to replicate Endeavour Energy's cost allocation approach. In that respect, the new amended CAM provides better understanding of the allocation of overhead costs, depot costs and non-system asset costs.

Other issues

Other amendments to Endeavour Energy's existing approved CAM are relatively minor. They include updated terminology to explain network switching costs, borrowing costs and income tax expenses. Also, descriptions of service groups are kept universal as it precludes the need to process further CAM updates in response to service classification changes.

Overall, we consider the impacts of the CAM amendments on Endeavour Energy's historical reported regulatory information will be trivial in nature. It is, nonetheless, appropriate for Endeavour Energy to update its CAM given its allocation of overhead costs and corporate changes.

3 Consistency with our Cost Allocation Guidelines

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

3.1 Endeavour Energy CAM assessment

The format and content of Endeavour Energy's CAM are regulated by clause 3.2(a) of our Cost Allocation Guidelines. Table 1 compares Endeavour Energy's proposed CAM against the requirements of clause 3.2(a). It also references relevant NER provisions and elements of our Ring-fencing Guideline.

Table 1 CAM assessment table

General obligations

| Rules | CAG | Requirements | Addressed |
|------------------|-------------|--|-----------|
| 6.15.4(a) | 1.5, 3.1(a) | DNBP must develop a proposed CAM for submission to the AER | Compliant |
| 6.15.4(b) | 1.5, 3.1(b) | DNBP's proposed CAM must give effect to and be consistent with the CAG | Compliant |
| | 5.4 | DNBP must maintain current copy of approved CAM on its website | Compliant |

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| CAG | Requirements | Addressed |
|-------------------|--|--|
| 3.2(a)(1) | Version number | CAM, p.2 |
| 3.2(a)(2) | DNBP's commitment to history and date of issue | CAM, p.2 |
| 3.2(a)(3) | Statement of nature, scope and purpose of document and way it is to be used | CAM, p.5 |
| 3.2(a)(3)A | Accountabilities for implementation | CAM, p.12 |
| 3.2(a)(3)B | Responsibilities for updating, maintaining and applying document and for internally monitoring and reporting its application | CAM, p.13 – Check "Records Management" |

| CAG | Requirements | Addressed |
|-----------|--|-------------------------|
| 3.2(a)(4) | Description of corporate and operational structure | CAM, p.4 |
| 3.2(a)(5) | Specification of service categories and types of persons to whom services provided | CAM, p.7 |
| 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 | CAM, section 2, pp.8-11 |
| 3.2(a)(7) | Description of how will maintain records of attribution and allocation | CAM, p.13 |
| 3.2(a)(8) | Description of how will monitor compliance with CAM and Guidelines | CAM, p.12 |
| 3.2(a)(9) | Commencement date | CAM, p. 4 |

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 | Compliant |
| | | 2.2.1(b)(1) | Include specified information on directly attributable costs to enable AER to replicate reported outcomes | Compliant |
| | | 2.2.1(b)(2) | Include specified information on shared costs to enable AER to replicate reported outcomes | Compliant |
| 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 | Compliant |
| 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 | Compliant |

| 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> | Compliant |
| 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 | Compliant |
| 6.15.2(5) | | 2.2.5 | Do not allocate the same cost more than once | Compliant |
| 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 | Compliant |
| 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 | Compliant |

4 Decisions

We consider the CAM amendments proposed by Endeavour Energy give effect to and are consistent with our guidelines and the rules. We therefore approve, under clause 6.15.4(c) of the rules, Endeavour Energy's proposed CAM amendments.

Appendix A: Endeavour Energy's CAM

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