



Jemena Electricity Networks (Vic) Ltd Revised Cost Allocation Method

AER Final Decision

May 2019

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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 Law
NEM	National Electricity Market
Rules, NER	National Electricity Market Rules
guidelines	Distribution Cost Allocation Guidelines

1 Introduction

1.1 Summary

On 2 April 2019 Jemena Electricity Networks (Vic) Ltd (JEN) submitted a revised Cost Allocation Method (CAM) — see Appendix A to this paper.¹ JEN provides electricity distribution services in north-west metropolitan Melbourne. A CAM is used to separately account for the costs of providing electricity distribution services, including from other services the distributor might provide. JEN has proposed its revised CAM take effect from 1 January 2021.

We have determined JEN's proposed 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 (distribution guidelines).

Accordingly, we have approved JEN'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 Victoria 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 Victoria.

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 services, comprising:
 - standard control services
 - alternative control services
- negotiated distribution services
- unclassified, or unregulated, 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 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 cost allocation between service classifications accurately and fairly represents costs incurred in providing those services. We rely upon historical and forecast

¹ Jemena Electricity Networks (Vic) Ltd, *Cost Allocation Method*, April 2019.

costs allocated in accordance with an approved CAM to determine prices charged, or revenues raised, by distributors such as JEN.

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

Following our approval, JEN's revised CAM will remain relevant to its statutory 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

JEN informally submitted a revised CAM on October 2019. We assessed the draft proposed CAM. Resulting from this assessment, JEN was provided with feedback that limited corrections were required to permit approval of the CAM.

JEN formally submitted its revised proposed CAM on 2 April 2019 for our approval. The results of our assessment of JEN's revised proposed CAM against the requirements of our guidelines are set out in section 3 of this paper.

2.3 JEN CAM revisions and structure

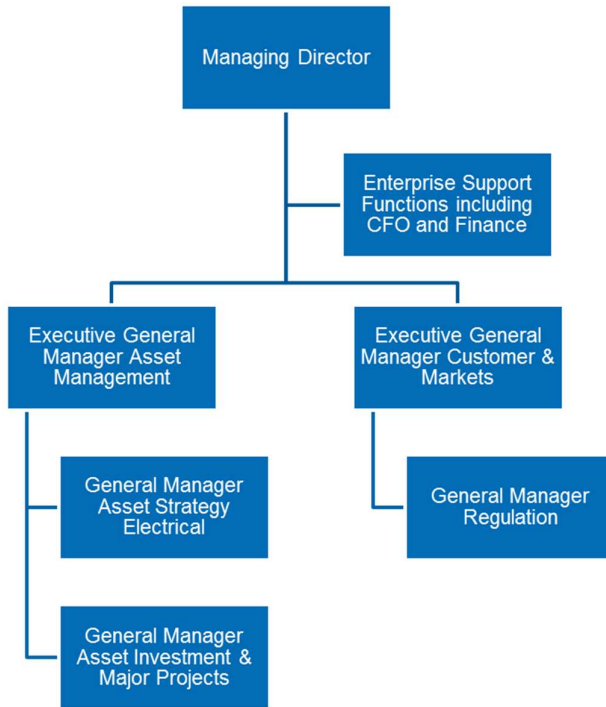
JEN sought AER approval of the attached amended CAM under clause 6.15.4(f) of the rules. The CAMs provide details on corporate structure, attribution of direct costs, allocation of indirect costs, cost recording and record keeping systems.

JEN submitted that the major reason it was revising its CAM was a change to its accounting practice from 1 January 2021. From this date JEN will expense rather than capitalise all corporate overheads (such as IT). JEN's revised CAM reflects this change in practice.

JEN also proposed to streamline the method of allocating shared costs. In the revised CAM, JEN states that it will allocate all shared costs (such as HR) based on each distribution service's proportion of direct costs. Previously, JEN used this allocator for some shared costs, but also used time writing and employee surveys to allocate some residual asset management costs. As an allocator, direct cost is simple to understand, straightforward to replicate and sufficiently causal. We support JEN's proposal to adopt direct costs as the sole shared cost allocator.

The amended CAM updates JEN's corporate structure information and provides additional information on its operational structure. All of JEN's enterprise support services are provided by Jemena Asset Management Pty Ltd. JEN's revised CAM includes details of Jemena Asset Management's operational structure in relation to JEN (see Figure 1 below).

Figure 1: Jemena Asset Management Pty Ltd operational structure²



Other amendments to JEN's existing approved CAM are relatively minor. They include updated details of responsibility within JEN for the application of the CAM and changes the description of distribution service categories to more generic terms. In JEN's existing CAM, specific services are listed; in the revised CAM, types of services only are described. We support this approach as it precludes the need to process further CAM updates in response to service classification changes.

² Jemena Electricity Networks (Vic) Ltd, *Cost Allocation Method*, April 2019, p. B-1

3 Consistency with our cost allocation guidelines

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

3.1 JEN CAM assessment

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

Clause 3.2(a) of the AER's Distribution Cost Allocation Guidelines	CAM references
(1)-(2) A version history and date of issue for the document	Compliant. See page ii.
(3) A statement of the nature, scope and purpose of the document and the way in which it is to be used by the distributor.	Compliant. See page 1.
(3) Details of the accountabilities within the distributor for the document in order to set out clearly: A. the distributor's commitment to implementing the CAM; and B. responsibilities within the distributor for updating, maintaining and applying the CAM and for internally monitoring and reporting on its application.	Compliant. See page 7.
(4) A description of the distributor's corporate and operational structure to enable the AER to understand how the distributor is organised to provide its distribution services.	Compliant. See pages A-1 and B-1.
(5) A specification of the categories of distribution services that the distributor provides to which costs are to be attributed or allocated and the types of persons to whom those services are provided.	Compliant. See page 2.
(6) The distributor's detailed principles and policies to be used for attributing costs directly to, or allocating costs between, categories of distribution services that meet the requirements of clause 2.2 of the Guidelines. For the avoidance of doubt, this includes the attribution or allocation of costs relating to any related party transactions.	Compliant. See pages 3 to 5.
(7) A description of how the distributor will maintain records of the attribution or allocation of costs to, or between, categories of distribution services to enable any such attribution or allocation to be: A. demonstrated to the AER, in accordance with clause 5.2 of these Guidelines; and B. audited or otherwise verified by a third party, including the AER, as required.	Compliant. See page 8.

(8) A description of how the distributor will monitor its compliance with the CAM and the Guidelines. Compliant. See page 9.

(9) Details of the proposed date on which the CAM will commence, having regard for clause 4.1(d) of these Guidelines. Compliant. See page vii.
