Submission

AEMC Consultation Paper

Economic Regulation of Network Service Providers – Transitional Arrangements

October 2012

AUSTRALIAN ENERGY REGULATOR

Overview

The Australian Energy Regulator (AER) welcomes the opportunity to respond to the Australian Energy Markets Commission (AEMC) consultation paper and draft rules on transitional arrangements for the AEMC's draft Chapter 6 and 6A Rules.

AER staff have undertaken discussions with stakeholders on alternative models that could be used to transition NSPs to the new economic regulatory framework. As far as has been possible, this submission seeks to bring together a consolidated approach following constructive engagement across the industry.

Section 1 of this submission considers the AER's high level objectives for transitional arrangements and the extent to which the AEMC's proposal meets those objectives.

Section 2 outlines the AER's preferred transitional model. In summary, this involves:

- Most of the upcoming round of revenue determinations being delayed by one year - but the next (full) regulatory control period would commence as scheduled instead of there being a separate 12 month transitional regulatory control period.
- Transitional rules would provide a mechanism for setting first year revenue (a placeholder revenue) that can then be trued-up over the remaining years of the regulatory control period when the final determination is made.
- The process of establishing the placeholder revenue, including consulting with stakeholders, should be as streamlined as possible, in recognition of the true-up that will follow.
- The aim of this process is to establish a placeholder revenue that moves prices in a direction likely to be consistent with the full regulatory determination process without undue price shocks for consumers, rather than to determine first year revenue with a level of precision.
- The new Rules, AER Guidelines and the Framework and Approach process would be used as a guide to estimating the placeholder revenue. The new regulatory framework would be used for the determination of the trued-up revenue for the full five years.

Further detail on this transitional model is contained in section 2. That section also describes why the AER considers that this model is preferable to other suggestions that have been raised in discussions on transitional arrangements to date.

Section 3 of this submission includes proposed treatment of a number of auxiliary matters for the first year of the transitional regulatory control period.

Section 4 outlines some areas where the transitional arrangements could provide flexibility to optimise the reset schedule.

The AER welcomes the AEMC's consultative approach to the transitional arrangements. The AER considers that the model proposed in this submission represents the best solution available having taken into account industry comments to date. The AER is willing to further discuss the issues raised in this submission with the AEMC if this would be of assistance.

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1 Key principles for an effective transition

1.1 Background

On 14 September 2012, the AEMC issued a consultation paper on the transitional arrangements that would be required to implement the draft Chapter 6 and 6A Rules. The AER welcomes the opportunity to provide this submission on the AEMC's consultation paper and associated draft transitional rules.

In the consultation paper, and at the public forum held on 26 September, the AEMC indicated that it was open to alternative suggestions for transitional arrangements, and encouraged parties to engage with each other in developing transitional arrangements that could achieve the objectives outlined by the AEMC in a simpler way.

AER staff have undertaken discussions with stakeholders on alternative models that could be used to transition distributors to the new economic regulatory framework. As far as has been possible, this submission seeks to bring together a consolidated approach following constructive engagement across the industry.

1.2 High level objectives

The AER has considered the transitional arrangements proposed by the AEMC against the following high level objectives:

- As much of the new rules as possible should apply to the upcoming round of determinations
- There is a need for time to develop new guidelines and schemes under the new rules
- There is a need to avoid congestion of reset work and framework development work
- Transitional arrangements should be as simple as possible
- There is a need to take into account revenue smoothing requirements, including the need to avoid undue price shocks for consumers.

1.3 AEMC's proposed transitional model

The AER broadly welcomes the direction of the transitional arrangements proposed by the AEMC as it seeks to achieve many of the high level objectives articulated above. That said the AER has been exploring alternative arrangements with stakeholders that that could better meet the objectives set out by both the AEMC and the AER.

1.3.1 Key benefits of the AEMC model

The AEMC consultation paper outlines that most of the upcoming round of revenue determinations would be delayed by one year, with a transitional determination required to set revenue for the 12 month interim period.

The AER agrees that it is necessary to delay most of the upcoming round of revenue determinations by one year[1]. This allows the new rules to apply to the upcoming round of determinations while leaving time for the AER and other stakeholders to participate in the development of the guidelines that are required under the new framework. Delaying businesses due in 2014, 2015, 2016 and 2017, rather than only those due in 2014, is necessary to avoid the creation of congestion in the reset timetable. If only the timing of initial resets was pushed back, the number of overlapping determination processes in electricity and gas, would make it difficult for businesses and other parties such as consultants to manage. Most importantly it would also inhibit other stakeholders such as consumers from effectively participating in these processes. For the reason outlined above, it is generally necessary to delay businesses due in 2017, however, Section 4 proposes some flexibility as to whether all of these businesses would be subject to a delay given possible changes to optimise the reset timetable. The AER has not yet finalised its position as to the appropriate transitional arrangements for SP AusNet transmission's next determination, which is due to come into effect from 1 April 2014. AER staff will continue to work with the AEMC and SP AusNet to determine whether a reasonable option exists that would achieve the general principle that the new framework should apply as soon as is possible.

Given a 12 month delay to most of the next round of resets is considered both necessary and appropriate, the question then turns to how to establish prices in the intervening period.

The AEMC proposal requires a nine month determination process to determine the prices that would apply for the 12 month period. Under the AEMC proposal that determination would apply for a separate transitional regulatory control period of 12 months, which would then be followed by a full determination process for the next five year regulatory control period.

While the AER accepts that this approach to setting prices for the 12 month period would achieve a transition to the new rules, the AER and other stakeholders have identified some issues with this process and have been working on alternative arrangements to achieve the underlying objectives in a simpler and more flexible way.

1.3.2 Scope for streamlining the transitional determination

In consultations with stakeholders, two main aspects of the model proposed by AEMC have been identified that could be streamlined.

First, the requirement for two determinations and two separate regulatory periods (and in particular the separate one year transitional regulatory control period) makes the transition from the old rules to the new rules potentially complex. In particular:

- A one year regulatory control period may create potential volatility in the price path, because any changes in revenue would need to be reflected within the year, rather than smoothed over a five year regulatory control period.
- Two separate determinations mean two different averaging periods for the cost of capital which creates additional complexity, including making it more difficult for businesses to manage their debt arrangements.

[1] Exceptions are those not delayed as part of the AEMC's transitional proposal (ElectraNet and interconnectors) as well as businesses due in 2017 that agree with the AER that the delay is not required – see section 4. The AER is yet to finalise its position on SP AusNet transmission.

Secondly, the arrangements for making a determination for the 12 month transitional period involve substantial engagement from the AER and businesses, at a time when parties would be focused on the development of key parts of the new framework. The determination process for setting one year of revenue is not dissimilar to a full determination process and would require significant resources from all parties. It may be possible to streamline these arrangements.

The AER considers that the priority in the transition period is the development of the new framework and the next round of 'full' regulatory determinations. Therefore, it has been engaging with businesses to see if it is possible to develop an alternative transitional model that achieves the AEMC's and the AER's objectives in a simpler way. The AER considers that the alternative model discussed below could satisfy the key objectives.

2 Alternative transitional model

The AER has developed the following model in consultation with NSPs. Initially, the AER held discussions with TransGrid and Transend on the basis of a proposal that was outlined by TransGrid at the public forum on 26 September. After some further development, TransGrid submitted a paper to the AEMC outlining that model, which the AEMC has published.

The model outlined below is the result of further discussions with a wide range of DNSPs and TNSPs (and with the AEMC) on the model originally proposed by TransGrid. The AER has attempted to take into account the views of NSPs in the development of this proposal and feels that it has addressed the issues raised during the consultation period. While there will be some matters where views differ between different NSPs, the AER considers this to be a comprehensive proposal that is preferable to the arrangements outlined by the AEMC and is likely to be acceptable to industry.

This section outlines key features of the proposed transitional model. Section 3 contains further information on auxiliary matters that need to be dealt with in the transition, including some that are specific to an NSP or a group of NSPs.

2.1 AER proposal

It is proposed that the next full (5 year) regulatory control period commence on its current schedule, but that the associated determination be delayed 12 months. A transitional decision would be required to establish revenue in the first 12 months, with that revenue being subject to a true-up mechanism when the determination is made 12 months later.

A key question then is how to establish prices in the intervening 12 month period.

The AER considers that it is desirable for the arrangements to establish transitional smoothed revenue that reflects and/or supports:

- the incorporation of as much of the new rules as possible, including having regard to the new rate of return guidelines from the start of the next regulatory control period;
- a revenue estimate for the first year of the regulatory control period that is consistent with the smoothed revenue that is likely to be determined through the delayed full regulatory determination process;
- a medium term price path that seeks to manage price and cash flow volatility over the regulatory period; and
- stakeholders having the opportunity to fully engage in the extensive consultation processes being conducted on the new guidelines in 2013.

2.1.1 Alternative arrangement for setting revenue for 12 month period

The current Rules already anticipate a circumstance where a regulatory determination is not made within a sufficient time for prices to be determined in the first year of a regulatory control period (see rule 6A.24.4). That rule provides for a streamlined alternative process for setting prices for the first year when no final determination has been made by the AER. Once the determination is made, there is a mechanism for a true-up to occur in following years to take account of the prices used for the first year.

This provides a useful general model for dealing with a 12 month delay in the making of a determination for the next round of resets. The transitional rules would need to provide a mechanism for setting first year revenue (a placeholder revenue) that can then be trued-up over the remaining years of the regulatory control period when the final determination is made.

Consistent with this approach, the process of establishing the placeholder revenue, including consulting with stakeholders, should be as streamlined as possible, in recognition of the true-up that will follow.

Placeholder revenue would be determined on the basis of a statement from the NSP submitted to the AER 5 months out from the start of the next regulatory control period. Regardless of the form of control that is to apply, it will be necessary to establish an indicative smoothed "placeholder revenue" requirement which will allow businesses to implement pricing arrangements for the assigned control mechanism in the transitional year.

The placeholder revenue statement would be supported by indicative range based information provided by the NSP, including:

- the forecast revenue in the last year of the current regulatory control period;
- the indicative opening regulatory asset base at the beginning of the next regulatory control period
- the possible indicative total and annual revenue requirements for the next regulatory control period based on indicative inputs including:
    - a range of indicative opex forecasts;
    - a range of indicative capex forecasts;
    - a range of WACC forecasts, taking into account recent regulatory decisions, available market information, expected market trends and having regard to the rate of return guidelines;
    - an indicative CPI;
    - a summary of overall plans for total expenditure over the transitional regulatory control period and an indication of how the placeholder revenue requirement fits within that plan; and
- any other inputs necessary for determining the placeholder revenue requirement or pricing arrangements for the transitional year.

For regulatory periods that commence after 1 July 2014, the regulatory determination timeline is proposed to be extended to allow for added consultation with stakeholders (the extended regulatory determination process). For these businesses, such as the distributors in Queensland, SA and Victoria, there would be no need for a separate placeholder revenue statement (supported by range based information). Rather their statement would form part of their substantive regulatory proposal and would be supported by information in the regulatory proposal including proposed revenue requirements and forecasts. As discussed below, the decision making process on the placeholder revenue would be the same regardless of whether it was on the basis of the placeholder statement or the regulatory proposal.

The aim of this process is to establish a placeholder revenue that moves prices in a direction likely to be consistent with the full regulatory determination process. It is recognised that the first year revenue will not be determined with a level of precision. Further, to minimise the potential for unacceptable price variations to customers both between regulatory control periods and during the regulatory control period, a consideration of the medium term smoothed price path may be appropriate.

All stakeholders appear to have an interest in minimising avoidable differences in the placeholder revenue and the revenue path eventually determined for the regulatory control period, particularly where this difference would represent unnecessary price increases for customers. To minimise the potential for unacceptable price variations over the whole period to customers, it will be important for the AER to consider the effect of setting a placeholder revenue that allows for a medium term smoothed price path from the current regulatory control period into the transitional regulatory control period.

It is expected that, to the extent they are in place, the new Rules, AER Guidelines and the Framework and Approach process would facilitate estimating the placeholder revenue. The new regulatory framework would be used for the determination of the trued-up revenue for the full five years.

2.1.2 Timing and process for setting placeholder revenue

For NSPs whose next regulatory period commences on 1 July 2014, placeholder revenue statements should be submitted to the AER at least 5 months prior to the start of this period. This will allow sufficient time for the AER to approve an appropriate revenue and for prices to be put in place prior to the commencement of the transitional regulatory control period.

As above, for NSPs that have the extended regulatory determination process applying, the revenue or proposed pricing statements would form part of their substantive regulatory proposal. This timing is considered to be preferable to other options including requiring a placeholder statement ahead of the substantive revenue proposal. Bringing forward in this fashion would increase the margin of error on the transitional revenue as it would be determined well before the start of the period. Additionally, delaying the implementation of the enhanced consumer engagement mechanism for all other networks is also not desirable.

Following submission of the statement on the placeholder revenue, the AER would publish an invitation for submissions from interested stakeholders. While this level of transparency is considered important, it is equally important for stakeholders to appreciate that the aim of this process is only to establish a placeholder revenue. The AER would not be forming a view on the merits of any particular forecast or building block parameter.

Underlining the transitional arrangements is a commitment between businesses and the AER to consult early on the indicative revenue requirement for the first year. However, if a suitable outcome is not reached through consultation, the AER's power to ultimately determine revenue is intended to provide a simple and quick mechanism for resolving that deadlock. As such, where the AER rejects the statement, the AER will be required to approve its own placeholder revenue for that NSP. Therefore, it is necessary for the AER to approve or reject the statement in sufficient time for prices to be set for the start of the regulatory control period. For TNSPs, the AER would publish the approved statement 3 months prior to the commencement of the first regulatory year of the transitional regulatory control period. For DNSPs, the AER would publish the approved statement 2 months prior to the commencement of the first regulatory year of the transitional regulatory control period. For DNSPs or TNSPs that have the extended process applying, the AER would publish a statement 4 months prior to the commencement of the first regulatory year of the transitional regulatory control period.

Where the AER is to establish a placeholder revenue, it is expected the AER would consider the following criteria:

(1) whether the DNSP's nominated placeholder revenue is supported by and consistent with the information the DNSP has provided and any other information available to the AER at the time which the AER considers relevant for the next regulatory control period;

(2) whether the placeholder revenue is likely to be broadly consistent with a distribution or transmission determination to be made by the AER for the transitional regulatory control period having regard to information provided by the DNSP, stakeholder submissions and any other information available to the AER at the time which the AER considers relevant;

(3) the desirability of minimising variations in expected revenue between regulatory periods and regulatory years;

(4) the desirability of minimising price variations for consumers between regulatory periods and regulatory years; and

(5) compliance with the control mechanism for the transitional year as set out in the Framework and approach paper applying to the *transitional regulatory control period*.

2.1.3 Other Timing Issues

Certain decisions and processes would need to be delayed for the transitional regulatory control period (that is, the first regulatory control period after the new rules come into effect). These transitional time limits would need to be addressed in the draft rules.

It is proposed that the following decisions be delayed for 12 months for the transitional regulatory control period:

- the due date for the Framework and Approach paper and all administrative steps in the development of that paper
- the submission due date for the NSP's proposal and any required associated documents
- the making of the AER's regulatory decisions on the proposal.

For NSW/ACT DNSPs where the Framework and Approach process has already commenced under the existing rules, the AER could publish a part of that paper in the first quarter of 2013, rather than waiting until November 2013 which would be the due date for the paper under the proposal above.

This would cover matters where there has not been a significant change from the existing rules and where the content has already been substantially developed – classification, control mechanisms and dual function assets. We understand that the relevant DNSPs would prefer the Framework and Approach paper on these matters to be published early so as to provide greater certainty. While there is already discretion to publish the paper early, the transitional arrangements should require the AER to segment the F&A paper into two parts and to be published at separate times. This would allow other matters to be set out in a second F&A paper in November 2013. The second F&A paper would cover incentive schemes, assessment methods and any other matters.

2.2 Other alternative models considered

The AER recognises that during the course of consultations with industry some other models have been raised. For the reasons outlined below, the AER considers that its model is preferable and is capable of achieving support from a wide range of stakeholders.

2.2.1 Mechanical approach to year one revenue

A number of stakeholders have suggested that the process for setting the placeholder revenue (assuming there is a true up) should go one step further in terms of simplicity. That is, it is argued that the AER's discretion to approve an appropriate placeholder revenue should be removed if preset criteria are met. The AER understands that variations of this model have been put forward including:

- Automatic approval of the proposed placeholder revenue if it is below a preset percentage of the expected final year revenue from the previous period

- A hybrid approach where the automatic approval above would apply, but if the business proposes something above the cap the AER approval process would apply.

The AER does not support these more mechanical methods for setting the placeholder revenue for a number of reasons. First it creates a default position of accepting revenues that may not any longer reflect efficient cost. For example, on the basis of current financial market conditions, a materially different rate of return is likely to be determined, when compared to the conditions that prevailed in the 2009 decisions.

Second, rolling forward expenditure at an existing or arbitrary level in the first year removes the need for a decision, but also removes the ability to take into account circumstances where a smoothed price path may be needed, including what price path may be needed given the likely movements over the full regulatory period. Establishing the placeholder revenue in the manner described in this submission allows year 1 revenues to at least estimate that likely revenue path, meaning that the true-up over the remaining years of the period is likely to be smaller. This will create a smoother price outcome for consumers.

The AER considers that some level of regulatory consideration is required to achieve this outcome. The risk of removing that consideration is that a circumstance may arise where a mechanical outcome produces an undesirable result.

2.2.2 Greater certainty on opex and capex allowances

Regardless of the model chosen for setting the placeholder revenue, there is broad support for a true-up to apply to the final determination to give effect to what is in essence a single 5 year regulatory period. As part of this, most businesses supported the AER approving an overall revenue requirement, rather than making a determination on individual components of the building blocks as part of the placeholder decision.

However, a consequence of having a true up at the time of the full determination is that there are no final capex and opex allowances determined until near the end of the first year of the regulatory control period. Most businesses described this level of uncertainty as manageable, noting that the application of incentive schemes in year one of the transitional period would not seek to penalise businesses for any difference between actual and forecast in year one. In order to completely remove this uncertainty, a more substantial process for setting year one revenue would be required, which would likely need to more closely reflect the arrangements that the AEMC originally proposed.

On balance, it appears that the industry considers that the placeholder and true-up model best balances between managing the year one risks and the issues associated with having two distinct regulatory control periods and associated determinations.

3 Auxiliary matters

Section two describes the AER's transitional model, including the proposed process for setting a placeholder revenue.

There will be some additional matters that need to be accounted for on a transitional basis for the first year of the regulatory control period while a full determination is being determined. These ancillary matters would include the operation of the incentive schemes, the operation of pass throughs and the pricing of alternative control services. The guiding principle that the AER has adopted in relation to these ancillary matters is that the rights and obligations of businesses in the current regulatory control period should generally be maintained until the full determination is made.

A number of specific matters could be dealt with as set out in the sections below.

To ensure that no matters are inadvertently missed in this process, the AER supports the adoption of a general catch all provision permitting the AER to determine that other rights and obligations of businesses that apply in the current regulatory control period shall continue to apply to the business until the full determination has been made.

3.1 Matters that generally apply to all NSPs

- To allow for efficient debt risk management, it is important that the determination process accommodates sufficient and timely certainty in terms of key approaches and processes. Accordingly, the published Framework and Approach paper could appropriately be used to establish any necessary processes for determining the rate of return, such as the timing of any 'sampling period'.

- Pass through events. Most pass through events are prescribed in the rules and they would continue to apply. The transitional arrangements would provide that, during the first year, NSPs would have access to the same pass through events on the same basis as apply in the current regulatory control period. The nominated pass throughs to apply from years 2 to 5 would be determined using the new rules in the full determination, which will allow for additional pass through events to potentially be nominated.

- Certain policy and framework papers, such as the *negotiating framework, Negotiated Service Criteria,* and the *pricing methodology*, would preferably continue to apply until a full regulatory determination is made, where these policies and frameworks already exist under a current determination.

- EBSS. Given that the expenditure target for year one of the period will not be determined until well into the year, rolling forward the EBSS is not appropriate. In addition, there is some uncertainty as to the future form of the scheme, with the ongoing application of the EBSS to be considered concurrently with the development of guidelines during 2013. The AER intends to set out its proposed approach to the application of the EBSS in the framework and approach paper process for each business – this would be confirmed in the final determination towards the end of year one of the transitional regulatory control period. Transitional rules should provide appropriate flexibility (through the guidelines or the F&A process) for the EBSS to apply differently in the initial year of the transitional regulatory control period. For example, it may be necessary to set the target in the first year equal to the actual for the purposes of the incentive mechanism. This would allow the scheme to operate in years 2 to 5, without creating any distortions in year 1.

- Any new capex incentive scheme as allowed under the draft rules would not apply in year 1 of the transitional regulatory period, but could apply in years 2-5 following the full determination.

3.2 Matters that apply to DNSPs

- Distribution STPIS scheme. The transitional rules should deem a rollover of existing arrangements to occur, unless the AER makes a different determination as part of the Framework and Approach paper. For example, target for year one could be deemed to be any target that applied in the last year of the previous regulatory control period, with the same amount of revenue at risk. Normal arrangements would apply for setting targets for years 2-5 as part of the full determination – the AER would set out its proposed approach in the Framework and Approach paper.

- Demand Management and Embedded Generation Connection Initiative Scheme (DMEGCIS) arrangements for year one would also be finalised as part of the Framework and Approach. The transitional rules should deem the following rollover of arrangements to occur, unless the AER makes a different determination as part of the Framework and Approach paper.

  For part A of the scheme, the transitional rules could deem an DMIA allowance in year one of the transitional regulatory period based on the average yearly DMIA amount provided (i.e. 1/5th of the total provided) in the prior regulatory control period for the current DMIS.

  Claw back amounts relating to the unused DMIA only occur in year two of the next period – so no transitional arrangement would be required. Part B of the scheme (foregone revenue related to projects approved under part A) would not be applied during year one of the transitional determination.

  If not already addressed in existing law, the transitional arrangements should ensure that carryover arrangements continue to operate – that is, benefits accrued in the existing regulatory period could be recovered in the next regulatory period where needed under the scheme. The demand management arrangements for years 2-5 would be set in the full determination process and the proposed approach would be set out in the framework and approach paper – which should allow for consideration of the outcomes of the AEMC's power of choice review. The AER could consider applying part B from year 2, depending on the control mechanism that is set.

- Treatment of Regulatory Asset Base in relation to shared assets would continue for year one of the transitional regulatory control period as per clause 11.16.3 of the NER.

- Connection policies will need to be dealt with on a jurisdictional basis.

- In relation to Alternative Control Services, unlike Standard Control Services, there is no avenue to 'true up' any variations. For the first year of the transitional regulatory control period – prices should be rolled forward with a CPI increase.

3.3 Matters that apply to TNSPs

- Transmission STPIS scheme. There are 3 components to the *proposed transmission STPIS scheme* – the service component, the market impact component and the network capability component. For the service component, it is proposed that the existing targets from the final year of the current control period are used and rolled forward until a full determination is made. For the market impact component, the new design of the scheme could be used from the commencement of the new regulatory period, including the placeholder year. This is an automatic calculation for setting the target based on the last 3 years of actual performance, which we agree to every year. This would not appear to require significant work for the TNSP or the AER at the time of the placeholder decision. The network capability component, which is new for this version of the scheme, could also potentially apply from the commencement of the new regulatory period. The role of the AER under this part of the scheme is limited as AEMO considers it before it is submitted to the AER. While the scheme is currently in draft form, minimal changes are expected prior to finalisation.

3.4 Matters that apply to specific NSPs or groups of NSPs

- Victorian DNSPs - The Victorian F-Factor scheme should be able to continue to operate in the first year of the transitional regulatory period by rolling over existing targets. The transitional rules would deem this to occur, unless the AER makes a different determination as part of the Framework and Approach paper. It would be implemented through a pass through arrangement consistent with the process in the current year until a new determination is made.

- Victorian DNSPs – Services currently regulated under the AMI Order In Council would continue to be regulated in accordance with that Order. To the extent that any transition is required at the expiry of the Order in council, these matter would be addressed through the Framework and Approach paper.

- NSW DNSPs - The existing arrangements for the operation of the D-factor scheme could be continued for year one of the next regulatory control period in NSW. Arrangements for the DMEGCIS are noted in the section above.

- NSW DNSPs – Businesses currently operating as a ‘paper trial’, without revenue at risk under the distribution STPIS could continue to do so in year 1 of the transitional regulatory control period.

- NSW DNSPs - NSW public lighting - Allowable public lighting price movements will need to be addressed for the transitional year. Details concerning the treatment of public lighting will need to be addressed through the Framework and Approach process. However, preliminary AER staff views are as follows. For assets constructed post 1 July 2009, the current approach will continue for the transitional year (that is, prices will be indexed by CPI). For assets constructed prior to 1 July 2009, the capital charges are decreasing as the RAB is depreciating with no new assets being added. Therefore an approach for the transitional year would be to take the 2013-14 total charge for each customer and apply that charge for 2014-15, subject to a later ‘true up’ process.

- Queensland DNSPs - The transitional arrangements provided for in clause 11.16.10 in relation to Queensland for Capital contribution policies would continue in year one of the transitional regulatory control period.

4 Optimisation of the reset schedule

The transitional rules could provide flexibility for adjustments to the reset schedule if more optimal arrangements can be agreed. The section below indicates two areas where the AER considers flexibility could be provided.

4.1 Flexibility to adjust the length of regulatory control periods

The AEMC's discussion paper recognises that given the new lengthened regulatory process timelines in the AEMC's draft Chapter 6 and 6A rules, the AER may, if given appropriate flexibility, seek to optimise the alignment of the determination schedule. In this regard, the AEMC proposes a transitional rule that would allow the AER, with the agreement of the NSP, to set a regulatory control period that is shorter than the existing five year minimum. The AER welcomes this transitional arrangement.

The drafting of this transitional rule would require a minor adjustment to take account of the AER's proposal that there would not be a separate 12 month transitional determination. If the AER's proposal is adopted, the transitional rule should allow the AER to set the transitional regulatory control period at less than five years, with the agreement of the NSP.

The AER notes that the AEMC has recommended in principle that TNSP resets be aligned. As noted in the AER's response to the Transmission Frameworks Review (TFR) second interim report, if the alignment of TNSP resets were to be pursued, the rules would need to provide sufficient flexibility for the AER to set shortened (and lengthened) regulatory control periods. This would not only allow for the potential alignment of TNSPs, but could also be used to deal with consequential impacts on the determination schedule more generally. Avoiding congestion in the determination schedule would be a key consideration as this would be difficult to manage for the AER and NSPs, and may inhibit the participation of consumers in the process.

The AER has commenced discussions with NSPs about potential optimisation to the reset schedule. This may include use of the AEMC's proposed transitional provision to set regulatory control periods of less than five years, where this is advantageous and can be agreed with the relevant NSP. However, these discussions may not be fully concluded by the time the transitional rules are determined.

4.2 Optional application of transitionals to NSPs due in 2017

Currently, under the AEMC proposal only ElectraNet's next determination (in 2018) would apply the new rules in full – other NSPs would have transitional arrangements designed to delay their next determination by a year. However, depending on the outcome of discussions with NSPs on optimising the reset schedule going forward, there may be circumstances where both the AER and an NSP that is currently due to be reviewed in 2017 wish to commence that next determination by applying the new rules in full instead of using the transitional arrangements to delay the reset by a year.

While the starting point would be that the transitional arrangements should apply to NSP resets currently due in 2017 to delay their next determination process by a year (and avoid overlap with earlier resets that are delayed by a year), it may not necessarily be appropriate for all NSPs due for review in 2017 to adopt the transitional arrangements. For example, under a scenario where the AER was to seek to align all TNSP resets on ElectraNet's current timetable in mid 2018, it may be advantageous to apply the transitional arrangements to delay Powerlink's next reset process by a year so that it is conducted at the same time as other TNSP resets. However, under this scenario, it would be worth considering commencing the Aurora determination on its current schedule, without applying the transitional arrangements to delay the reset by a year. This would avoid Aurora's reset aligning with the TNSP resets.

A possible solution would be for the transitional arrangements that delay determinations processes by 12 months to apply to businesses due for review in 2017 unless the NSP and the AER agrees (sufficiently ahead of time) that the transitional rules would not apply to the NSP's forthcoming determination. Alternatively, the default position of applying the transitional rules to all NSPs could apply, with a subsequent rule change being submitted if a more preferable reset scheduling option emerged.