

Attachment L: Other compliance matters



1. Reporting on recovery of designated pricing proposal charges

Designated pricing proposal charges include the transmission related charges payable to TransGrid, avoided TUOS charges payable to certain generators as well as inter distributor payments.

Relevant rule requirements

For the transitional period, the transitional provision 11.56.3(a)(14) requires the AER to:

*“specify as the manner in which the affected DNSP is to report to the AER on its recovery of **designated pricing proposal charges** and jurisdictional schemes amounts, the manner that was decided for the current regulatory control period of the affected DNSP, except to the extent the designated pricing proposal charge or jurisdictional scheme was not subject to such a decision for that current regulatory control period, in which case the manner or reporting must (to that extent) be as decided by the AER in the distribution determination for the transitional regulatory control period..”*

While clause 11.56.3(a)(15) requires the AER to:

*“specify as the adjustments to be made to subsequent pricing proposal to account for over or under recovery of any **designated pricing proposal charges** or jurisdictional scheme amounts, the adjustments that were decided for the current regulatory control period of the affected DNSP, except to the extent the designated pricing proposal charge or jurisdictional scheme was not subject to such a decision for that current regulatory control period, in which case the adjustments must (to that extent) be as decided by the AER in the distribution determination for the transitional regulatory control period”*

For the reasons explained below no formal decision has been made by the AER in relation to the reporting on the recovery of designated pricing proposal amounts and adjustments in subsequent pricing proposals so the AER must make a decision for the transitional regulatory year.

Arrangements for the 2009-2014 period

Under the transitional rules which applied to the current period (2009-2014), Rule 6.12.1(19) provided for broadly the same decision but required the AER to make a decision in relation as to how the DNSP was to report on the recovery of transmission use of system charges and on the adjustments to be made in future pricing proposals, rather than designated pricing proposal charges. As part of its decision for the 2009-2014 the AER imposed requirements for Ausgrid to maintain a transmission use of system (TUOS) overs and unders account. These requirements were set out in detail in appendix I to that decision.

Proposed Arrangements for 2014-2019 period

Ausgrid proposes that the AER make a decision which results in the same mechanism for the reporting on recovery of designated pricing proposal charges and subsequent adjustments to that used for transmission use of system charges during the 2009-14 regulatory period. The current mechanism is based on the audited closing balance in year t-2, and an estimate of the closing balance in year t-1. The over/under recovery in year t-1 is recovered via an adjustment in year t. This information is reported in the form of a table in the pricing compliance model, submitted to the AER as part of the annual pricing proposal. An example based on the requirements of attachment I of the AER's 2009-14 decision for Ausgrid is shown in table 1.

Table 1 - Proposed reporting on recovery of designated pricing proposal charges (FY2014 overs and unders account set out in 2013-14 pricing proposal used as an example)

Ausgrid - financial year ending 2014

TRANSMISSION RECOVERY ARRANGEMENTS

1A

Inputs		t-2 audited 2012	t-1 expected 2013	t forecast 2014
Financial year ending				
Revenue from Transmission Cost Recovery (TCR) Tariffs	\$'000	491,661	514,900	550,675
			-	-
Transmission charges to be paid to TNSP's	\$'000	485,056	523,073	516,500
(Settlement residue payments)	\$'000	-	-	-
Avoided TUOS payments	\$'000	274	500	500
Inter-distributor payments	\$'000	13,170	13,500	13,838
Total transmission related payments (net of settlement residue)	\$'000	498,500	537,073	530,838
		-	-	-
Audited opening balance of trans overs/(unders) account	\$'000	10,118	-	-

1B

Overs and Unders Account forecast closing balance		t-2 audited 2012	t-1 expected 2013	t forecast 2014
Financial year ending				
Interest rate applicable to balance	%	10.02%	10.02%	10.02%
Opening balance	\$'000	10,118	3,949	(18,912)
Interest on opening balance (365 days)	%	1,014	396	(1,895)
forecast over / (under) recovery for financial year		(6,840)	(22,173)	19,837
Interest charged on over/under recovery for financial year	\$'000	(343)	(1,084)	970
Closing balance of transmission overs/ (unders) account	\$'000	3,949	(18,912)	0.0

2. Reporting on jurisdictional scheme amounts (climate change fund)

Jurisdictional schemes amounts are amounts which DNSPs are required to pay under jurisdictional requirements which have been recognised by the rules or the AER as amounts which may be recovered under the rules as part of the DNSP's pricing proposal. There are currently two jurisdictional schemes relevant to the NSW DNSPs which are recognised by the rules. The first is the NSW solar bonus scheme, the second is the NSW climate change fund, each of which are recognised under rule 6.18.7A(e)(2) and (3) respectively.

For the transitional regulatory control period, the transitional provision 11.56.3(a)(14) requires the AER to:

*specify as the manner in which the affected DNSP is to report to the AER on its recovery of designated pricing proposal charges and **jurisdictional schemes amounts**, the manner that was decided for the current regulatory control period of the affected DNSP, except to the extent the designated pricing proposal charge or jurisdictional scheme was not subject to such a decision for that current regulatory control period, in which case the manner of reporting must (to that extent) be as decided by the AER in the distribution determination for the transitional regulatory control period.*

While clause 11.56.3(a)(15) requires the AER to:

*specify as the adjustments to be made to subsequent pricing proposal to account for over or under recovery of any designated pricing proposal charges or **jurisdictional scheme amounts**, the adjustments that were decided for the current regulatory control period of the affected DNSP, except to the extent the designated pricing proposal charge or jurisdictional scheme was not subject to such a decision for that current regulatory control period, in which case the adjustments must (to that extent) be as decided by the AER in the distribution determination for the transitional regulatory control period*

For the reasons explained below no decision has been made by the AER in relation to reporting on the recovery of jurisdictional scheme amounts and adjustment in subsequent pricing proposals so the AER must make a decision for the transitional regulatory year.

Arrangements for the 2009-2014 period

During the 2009-2014 period all payments made under the NSW solar bonus scheme have been recovered by NSW DNSPs through payments to and from the NSW climate change fund. Clause 6.18.7 of the transitional chapter 6 expressly provided for pricing proposals to pass on to customers, payments into the climate change fund. Once payments were made into the climate change fund the NSW government arranged for the NSW DNSP to be reimbursed from the fund. Clause 6.18.7 was amended into its current form when amendments were made to the rules in July 2010 by the National Electricity Amendment (payments under feed-in schemes and climate change funds) Rule 2010. Consequently the AER has not been required to make a formal decision on reporting on the recovery of jurisdictional scheme amounts for Ausgrid.

Proposed arrangements for the 2014-2019 period

The NSW DNSPs anticipate that the current arrangements will continue whereby Solar Bonus Scheme payments are recovered through the climate change fund until the NSW solar bonus scheme finishes in December 2016. However should there be any change to these arrangements, the NSW DNSPs would need to recover NSW solar bonus payments directly as a jurisdictional scheme. Consequently the NSW DNSPs are seeking that the AER make a decision on how the NSW DNSP are to report on the recovery of both the NSW climate change fund and the NSW solar bonus scheme and any subsequent adjustments.

Ausgrid proposes that the AER makes a decision that results in the same mechanism for the reporting on recovery of jurisdictional scheme amounts and adjustments in subsequent pricing proposals for both the NSW climate change fund and the NSW solar bonus scheme as that which has been in place during the 2009-14 regulatory period.

The current mechanism is based on the audited closing balance in year t-2, and an estimate of the closing balance in year t-1. The over/under recovery in year t-1 is recovered via an adjustment in year t. This information is reported in the form of a table in the pricing compliance model, submitted to the AER as part of the annual pricing proposal. An example is shown in table 2.

Table 2 - Proposed reporting on recovery of climate change fund and NSW solar bonus scheme charges (FY2014 overs and unders account as set out in 2013-14 pricing proposal used as an example)

Ausgrid - financial year ending 2014

CLIMATE CHANGE FUND RECOVERY ARRANGEMENTS

2A

Inputs		t-2 audited 2012	t-1 expected 2013	t forecast 2014
Financial year ending				
Revenue from Climate Change Fund Recovery.	\$'000	71,331	118,100	149,704
		-	-	-
Climate Change Fund Contribution	\$'000	71,012	118,000	149,802
		-	-	-
Audited opening balance of CCF overs/(unders) account	\$'000	(313)	-	-

2B

Overs and Unders Account forecast closing balance		t-2 audited 2012	t-1 expected 2013	t forecast 2014
Financial year ending				
Interest rate applicable to balance	%	10.02%	10.02%	10.02%
Opening balance	\$'000	(313)	(10)	94
Interest on opening balance (365 days)	%	(31)	(1)	9
forecast over / (under) recovery for financial year		319	100	(99)
Interest charged on over/under recovery for financial year	\$'000	16	5	(5)
Closing balance of transmission overs/ (unders) account	\$'000	(10)	94	0.0

3. Demonstration of compliance with control mechanism for standard control services

This section provides our proposed approach to demonstrating compliance with the control mechanism for distribution standard control services. This section also provides the AER with:

- Our consideration of how the over/under recovery of revenue should be calculated for the transitional year
- An understanding of some of the key outstanding issues in relation to the control mechanism.

Proposed control mechanism for distribution standard control services

The AER proposed formula for the revenue cap is shown below:

$$MAR_t = \sum_{i=1}^n \sum_{j=1}^m p_{ij}^t q_{ij}^{t*}$$

$$MAR_t = AR_t + I_t + T_t + B_t$$

$$AR_t = AR_{t-1}(1 + CPI)(1 - X_t)$$

Where:

- MAR_t is the maximum allowable revenue in year t.
 p_{ij}^t is the price of component i of tariff j in year t.
 q_{ij}^{t*} is the forecast quantity of component i of tariff j in year t.
 AR_t is the allowable revenue for year t.
 I_t is the sum of incentive scheme adjustments in year t¹.
 T_t is the sum of transitional adjustments in year t.
 B_t is the sum of annual adjustments in year t.
 CPI_t is the percentage increase in the consumer price index.
 X_t is the X-factor in year t.
 AR_1 is the allowable revenue in the first year of the regulatory control period.

It is important to note that there are many aspects to the above control mechanism formula that have not yet been decided by the AER.²

Over/under recovery in the transitional year

As noted above, Ausgrid considers that the amount determined by the AER as the annual revenue requirement for the transitional year in its distribution determination for the transitional regulatory control period should be the amount used in calculating the over/under recovery of revenue for 2014-15.

However, the approach of recovering the additional revenue of the transitional year for certain ancillary network services and unclassified services complicates this calculation of over/under recovery of revenue for standard control services. The complication arises because Ausgrid does not have the system capabilities to accurately disaggregate the revenue collected in 2014-15 between revenue for standard control services, revenue for alternative control services and revenue for unclassified services.

This means that Ausgrid is unable to provide an accurate actual amount of revenue collected for standard control services to compare against the allowed revenue approved by the AER in its determination for the transitional proposal.

This issue arises for the transitional year only because the DUOS price is a bundled price that recovers not only the allowed revenue for standard control services but also the additional revenue for certain ancillary network services and unclassified services. This issue would not occur for the subsequent years as we would be transitioning to separate charges for standard control services and alternative control services.

Ausgrid considers the most practical resolution to this issue is to deduct the additional revenue amount for certain ancillary network services and unclassified services used to calculate the bundled DUOS charges in the transitional

¹ We propose the I factor to include the recovery of expenditure arising from the application of the current D-Factor scheme to account for the two year lag. That is, the D-Factor outcomes for 2012-13 and 2013-14 will be accounted for in 2014-15 and 2015-16 respectively.

² AER 2013, Formulae for control mechanisms – revised, Matters relevant to the framework and approach for NSW and ACT DNSPs 2014-19, February, p.7

year from the total actual revenue collected for the transitional year. To avoid doubt, we set out an example in table 3.

Table 3 - Calculation of over/under recovery in the transitional year³

2014-15	Revenue used for calculation bundled DUOS price	Actual revenue collected from charging bundled DUOS
Revenue approved by the AER as annual revenue requirement in the transitional determination	\$200	
Additional revenues for certain ACS and unclassified services	\$50	\$280
Total bundled revenue	\$250	

To calculate the over/under recovery of revenue for the transitional year, the actual revenue for standard control services would be calculated as the difference between \$280 and \$50 (i.e. 280 less 50 = 230) as outlined in table 3. This amount (230) will be taken to be the actual revenue collected for standard control services for the transitional year and will be used to calculate the over / under recovery. In this case it will be an over recovery of \$30

For clarity, the allowed revenue to be used for under / over recovery is the amount determined in the determination for the transitional period and not the amount approved for the transitional year in the determination for the subsequent period. The difference between the amounts determined in these two determinations has already been accounted for by adjusting the ARR for the subsequent years.

Ausgrid's position on managing price stability issues through the application of tolerance limits

Ausgrid and the other NSW DNSPs expressed their concern over the potential risk under the revenue cap control mechanism for unanticipated changes in our volume environment that result in our customers being exposed to increased price uncertainty.⁴ We note that the AER shares our concerns and proposes to address this issue by applying tolerance limits to the design of the overs and unders account mechanism to smooth the adjustments to prices during the course of the regulatory control period.⁵

Ausgrid believes that in the current uncertain volume environment it is in the long-term interest of electricity customers for the level of tolerance limits to be sufficiently generous to enable the NSW DNSPs to smooth price adjustments that arise from both random influences (such as weather) and structural influences (such as uptake of energy efficient appliances, solar PV systems and gas). Ausgrid's preliminary analysis of the potential impacts of our volume risk exposure on pricing outcomes under the revenue cap indicates that this tolerance limit would need to be in the order of 5% of the annual revenue requirement.

It is also important that there are appropriate arrangements in place to deal with a situation where the actual over or under recovery of revenue in period t-2 exceeds the prescribed tolerance limit. Ausgrid's preference would be for the AER to adopt a light handed approach involving an obligation being imposed on the DNSP to develop a plan to address the issue over a reasonable time frame. The AER should assess the plan on the basis of explicit criteria to ensure that the DNSP has a clear understanding of how best to address this issue. We consider the key criteria will need to provide sufficient guidance to the DNSP to develop a plan that strikes an appropriate balance between satisfying the short-term need of customers for price certainty with the longer term need to avoid unacceptable transitional pricing issues across the regulatory control period. We are keen to work with the AER to ensure that this important design feature of the control mechanism is appropriately addressed in the AER's distribution determination

Ausgrid's position on the need for an annual audit of volume and the transmission closing balance in year t-2

Ausgrid believes that there is merit in continuing the audit process that was undertaken for the weighted average price cap (WAPC) in the current regulatory control period. This audit process is well understood by Ausgrid and the other NSW DNSPs and provides adequate independent assurance to the AER in relation to the key actual inputs to the compliance process, such as the closing balance on the Transmission overs and unders account in year t-2 and the actual volumes at the tariff component level in year t-2.

Ausgrid does not support an independent audit of the estimate of volumes at the tariff component level in year t-1 and the forecast of volumes at the tariff component level in year t. This is because the revenue cap provides a clear incentive for the DNSP to adopt the most accurate volumes given that there is no long-term gain from doing otherwise.

³ Numbers used in this example are for illustrative purposes only

⁴ Ausgrid, Endeavour Energy and Essential Energy, NSW DNSPs' response to the AER's preliminary framework and approach paper, 17 August 2012, p. 34.

⁵ AER 2013, stage 1 framework and approach – NSW electricity distribution network service providers, March, p.52

