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Mr Chris Pattas
General Manager – Network Operation and Development
Australian Energy Regulator
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Dear Mr Pattas,

DRAFT SHARED ASSET GUIDELINES AND EXPLANATORY STATEMENT

Ergon Energy Corporation Limited (Ergon Energy), in its capacity as a Distribution Network Service Provider (DNSP) in Queensland, welcomes the opportunity to provide a submission to the Australian Energy Regulator (AER) on its *Draft Shared Asset Guidelines and Explanatory Statement*.

Ergon Energy provides in principle support for the general approach taken by the AER in the Draft Guidelines and Explanatory Statement. In particular, the Draft Guidelines are clear that the shared asset mechanism applies only where established assets provide both Standard Control Services (SCS) and unregulated services, but whose costs are only allocated to SCS; or where assets for which the initial cost allocation under an approved Cost Allocation Method (CAM) comes to understate its use to provide unregulated services. However, Ergon Energy believes that the Guidelines would benefit from providing greater clarity to the definitions of *return on capital*, *return of capital*, and *shared asset unregulated revenues*, as they apply to the cost reduction method and control step.

Ergon Energy is a member of the Energy Networks Association (ENA), the peak national body for Australia's energy networks. The ENA has prepared a comprehensive submission addressing the AER's Draft Guidelines and Explanatory Statement, and proposes the AER reconsider some of its propositions which may limit the utility of the Guidelines. To that extent, the ENA proposes amending parts of the Guidelines in relation to cost allocation and shared assets; alternative cost reduction methods proposed by service providers; reporting of contractual information; and services which use shared assets only marginally. Ergon Energy is fully supportive of their submission.

In particular, Ergon Energy supports the ENA's proposal that the Guidelines reflect statements made in the Explanatory Statement relating to services which use shared assets only marginally. In section 3.3.1 of the Explanatory Statement the AER suggests network service providers can apportion unregulated revenues to reflect the extent to which unregulated services rely on shared assets. However, this does not appear in the Draft Guidelines. Furthermore, Ergon Energy would like to express that the 'marginal use' apportionment is likely to be applied more frequently rather than 'in the extreme'.

Ergon Energy currently applies transitional clause 11.16.3 of the National Electricity Rules for the treatment of its Regulated Asset Base (RAB), such that assets that are used to provide SCS, as well as unregulated services or other Alternative Control Services (ACS) (excluding street lighting or new large customer connection assets) are included in their entirety in the RAB. Ergon Energy identified the following categories of assets that are marginally used in this context in the 2010-15 regulatory control period: Buildings; Motor vehicles; Computer software; and Office machines/furniture and equipment and inventories.

To ensure that the full cost of the shared asset used is borne by the beneficiary, Ergon Energy applies an internal charge (incorporating direct and indirect costs of asset usage; depreciation; and return on assets) in relation to the marginal usage of the RAB assets for other ACS and unregulated services. Ergon Energy notes that the current transitional arrangements will cease and Ergon Energy will be subject to the Guidelines at the start of the next regulatory control period. Notwithstanding, Ergon Energy believes that the 'marginal use' apportionment will have validity in a large number of cases.

For example, Ergon Energy operates an isolated network which is not subject to economic regulation by the AER. While the majority of the assets used to provide this service are not included in the RAB there is a minor use of communications and buildings, and occasional but limited vehicle usage.

During the 2010-15 regulatory control period, an average annual adjustment of $3.36 million was made, compared to total average annual revenues of $1361 million. Therefore, only 0.25 per cent of annual revenues are attributable to unregulated and ACS services. Given that the Guidelines only relate to unregulated revenues, this amount will be even more marginal. As such, Ergon Energy supports the ENA's proposal that the statements made in the Explanatory Statement relating to shared assets only marginally are also reflected in the Guideline; and that the AER revise their position on the frequency with which this may be applied.

Moreover, Ergon Energy suggests that where a service provider uses an alternative method to calculate a cost reduction, they must demonstrate that the proposal is consistent with the National Electricity Objective, rather than demonstrating that consumers would be 'no worse off'. Ergon Energy also supports the ENA's proposal that where a different method is proposed, the service provider should demonstrate that this method provides for a more accurate reflection of the extent of double recovery of shared asset costs, compared to the method set out in the Guidelines. Either of these proposals offer a pragmatic approach to an alternative methodology.

Furthermore, Ergon Energy agrees with the ENA's suggestion that the Shared Assets Principles do not prohibit consideration of incremental costs. As such, an alternative method proposed by a service provider should not be discounted on the basis of the use of incremental costs in their methodology.

Should you require any additional information or wish to discuss any aspect of this submission, please do not hesitate to contact either myself on (07) 4092 9813 or Trudy Fraser on (07) 3851 6787.

Yours sincerely

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