9 November 2018

Mr Moston Neck
Australian Energy Regulator
Level 2, 400 George Street
Brisbane QLD 4000

Dear Moston

Preliminary framework and approach

Thank you for the opportunity to comment on the Australian Energy Regulator's (**AER**) preliminary framework and approach for Victorian distributors. In general we consider the positions outlined will support effective regulation over the 2021–2025 regulatory period. In the below attachment we have outlined some concerns and comments with respect to the:

- classification of services
- form of control formulas
- application of a small scale incentive scheme.

We welcome the opportunity to discuss this submission with the AER. Please contact Frans Jungerth on 03 9683 2022 or fjungerth@powercor.com.au if you have any questions.

Yours sincerely

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1 Service classification

1.1 Connections

We support the proposed connection service classifications outlined in the preliminary framework and approach. In particular that:

- basic connections are classified as alternative control
- standard and negotiated connections are classified as standard control.

In contrast, we would not support the connection classifications outlined in the AER's Service Classification Guideline 'baseline list of services' being applied in Victoria.[1] In the baseline list, standard and negotiated connections are separated into three components, with the 'premises connection' component being classified as alternative control. For the reasons outlined below, we consider all components of standard and negotiated connections should be standard control.

Rural customers

Many rural customers, including farm properties, require negotiated connections because the network does not extend to their premises. If network extensions located on private land were to be considered as 'premises connections' and classified as alternative control, these customers' connection charges would increase. The following table shows the impact of changing classification for sample of rural connections in 2018 requiring pole extensions on private land.

Table 1 Additional connection costs for rural customers under an alternative control classification

Customer type	Average increase in connection charges under ACS classification
Rural residential	$4,500
Rural commercial (farm buildings, irrigation etc)	$44,300

Source: Powercor connections data

Rural customers may already face material connection charges due to their remoteness and we believe these increases would not be in our customers' interests.

We note that by design, making a standard control connection that is subject to the cost-revenue-test will not increase the distribution use of system charges to other customers. That is, while maintaining a standard control classification results in a different financial outcome to an alternative control classification, it is still cost reflective and doesn't result in cross subsidies. We therefore consider a standard control classification is appropriate and consistent with the 'efficient connection' and 'equitable' principles outlined in the AER's Service Classification Guideline.[2]

Large customers

For large customers there is not a clear distinction between premises connection and extension works. Large customers typically require a distribution substation on their premises. These are sized in increments and so

[1] AER, Electricity Distribution Service Classification Guideline September 2018, p. 20.

[2] AER, Electricity Distribution Service Classification Guideline, September 2018, p. 19.

customers always receive additional capacity, which we use to help manage network load. Therefore even the works on private land are shared network works, rather than a dedicated premise connection. [3]

Additionally, given there is no clear distinction between premises connections and extensions, there is no way to split the connection's cost into alternative control and standard control services. Further, we do not have systems or processes in place to split these connections/revenue into multiple classifications. Therefore we seek the whole connection be standard control.

Contestability

In September 2018 the Essential Services Commission (Victoria) (**ESC**) concluded a review of electricity connection processes.[4] The recommendations included:

> *'Each distributor to use the AER Service Classification process at the beginning of each price review (NER Chapter 6) for the AER to seek appropriate service descriptions and service classifications to facilitate competition.'*

We believe the service classifications outlined in the preliminary framework and approach are appropriate to facilitate competition. While negotiated connections would be standard control, we apply a rebate scheme and a real estate developer equalisation scheme. As previously outlined these ensure competitive neutrality regardless of classification.[5]

1.2 Metering services

Meter exit service

In our request for a replacement framework and approach we sought metering exit services, however the service was not included. We request this service be included in the final framework and approach.

The purpose of an exit fee is to retire the remaining depreciated value of a meter and associated communications and IT systems, for a meter that is removed from a premises.

When a brownfield site converts to an embedded network, we must remove our type 5 (Advanced Metering Infrastructure (**AMI**)) meters from the site. This is because an embedded network takes bulk supply from us at a single point and is then responsible for the metering beyond that point e.g. the customers' metering within an apartment building.

Type 5 metering is regulated as alternative control (revenue cap). Without an exit fee, all other metering users bear the undepreciated value of the meters and share of metering infrastructure that is no longer required because the embedded network has sought to provide its own metering service. In this scenario, the exit fee would be levied on the party establishing the embedded network.

Similarly, if metering services in Victoria become contestable, customers may choose to have a new meter provided by the competitive market. At this time, the customer would stop paying for their regulated type 5 meter, even though its full cost was incurred to service the customer. All other metering customers would bear the undepreciated value of the customer's meter and share of the AMI infrastructure without an exit fee.

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[3] Works beyond the distribution substation are the customers' responsibility, hence they are not premise connection works.

[4] <https://www.esc.vic.gov.au/electricity-and-gas/electricity-and-gas-inquiries-studies-and-reviews/electricity-connections-process-review-2018#tabs-container2>

[5] CitiPower, Powercor and United Energy, response to the AER's service classification draft guideline, 25 July 2018.

We note that provision for meter exit fees is in place for the 2016–2020 regulatory period and was included in the Victorian Government's metering Order in Council. We therefore seek the AER to include the following service description in the 'auxiliary metering services' group:

'meter exit services for the recovery of undepreciated meter and meter infrastructure costs'

Type 7 meter services

In the preliminary framework and approach the AER has classified type 7 metering services as alternative control (fee based). In the AER's stakeholder forum, the AER noted it was considering reclassifying the service as standard control, consistent with the classification in other States.

We propose type 7 metering services be including in the 'Type 5 and 6 (inc. smart metering) services where the distributor remains responsible' group. This would mean type 7 metering services would be alternative control and subject to a revenue cap.

While type 7 installations do not have a physical meter, the systems used to provide the services are the same as those used for other metering. That is, type 7 metering services use the same AMI network management system and meter data management system that are used to distribute metering data out from the business to the market. Therefore we consider it would be appropriate to use the same method and model used to determine type 5 meter charges, to determine type 7 metering service charges— however the hardware cost of the meter would be excluded.

By including type 7 metering in this group, customers requiring type 7 metering services would pay their fair share of the systems used in their metering. Additionally, the revenue we receive would reduce the metering regulatory asset base and (appropriately) reduce the metering costs of other customers.

Meter auxiliary service

Under the 'auxiliary metering services (type 5 and 6 including smart metering) where the distributor remains responsible' group the activity 'non-standard metering services for Type 5 to 7 meters' is included. We consider the group name should be broadened to reference type 7 meter services.

Should the AER accept our above positon that type 7 meters be part of the metering revenue cap, that group would also need to be renamed to include reference to type 7 meter services.

1.3 Fast track audit

The ESC's review of electricity connection processes recommendations included:

'Each distribution business will seek appropriate service descriptions and classifications for audit services as part of the AER Service Classification process for the 2021-25 Victorian electricity distribution price review (for example, each will consider 'fast-tracked audit services', and 'audit revisits', as possible alternative control services).'

The AER's preliminary framework and approach includes an 'inspection and auditing services' group classified as alternative control. We believe this group provides us with the scope we need to meet the ESC's recommendation. In particular:

- an alternative control classification is appropriate as audit costs should be paid by the customer requesting the service, however, there is still regulatory oversight and approval of the charge rate
- we understand the AER's 'further description' of the services are not exhaustive and there is scope to include a fast-track audit fee in our General Service Charge Pricing Schedules
- the service group makes provision for audit revisits.

We therefore accept the AER's service description and classification in this respect.

1.4 Embedded networks

At the Victorian distributors' request, the AER outlined its intention to include a service for processing embedded network requests.[6] We believe, due to an oversight, this was omitted from the 'connection application and management services group'. We request the AER include this service.

2 Form of control formulas

2.1 Inflation

In each of the price control formulas, the CPI term is based on the December quarter. Unlike in other States, Victorian distributors' regulatory period is set on calendar years. Due to this, the CPI term should be based on the June quarter because our annual pricing submissions are due in September, which is before the December CPI is available.

2.2 Depreciation

We agree with the preliminary framework and approach that forecast depreciation should be applied. We believe, however, the framework and approach should clarify what we believe to be the AER's intent that forecast depreciation only apply to standard control services. Similarly, we believe the framework and approach should clarify the incentive schemes apply to standard control services.

For the metering revenue cap, we propose actual depreciation be applied. In the absence of the Capital Efficiency Sharing Scheme (**CESS**) applying to alternative control services, applying actual depreciation ensures there is an incentive on distributors to deliver metering services efficiently. This is consistent with the current approach and the AER's comment that:[7]

> *'Our approach is to apply forecast depreciation except where: there is no CESS in place and therefore the power of the capex incentive may need to be strengthened …'*

2.3 Continent projects and pass throughs

The price control formula does not discuss the way in which contingent projects are to be included. We seek the AER to make provision for these projects as they form an important part of the regulatory framework.

Additionally, the proposed metering price control does not make provision for pass-throughs. Metering is an area which has historically faced many changes. Most recently this included changes to the frequency of recording metering data and data storage requirements.[8] Due to the timing of this change, in this case the required revenue can be included in the 2021–2025 regulatory proposal, however, changes may also occur within the regulatory period. Given this, we request that provision for pass-throughs be made in the metering price control formula.

3 Small scale incentive scheme

We are considering adopting a small scale incentive scheme as proposed by AusNet. Before doing so we will need to further engage with our stakeholders, including the Consumer Challenge Panel, to understand whether

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6 AER, Preliminary framework and approach, September 2018, p. 35 & 35.

7 AER, Preliminary framework and approach, September 2018, p. 85 & 86.

8 AEMC, Rule determination; National Electricity Amendment (Five Minute Settlement) Rule 2017, 28 November 2017.

it has our customers' support. We will keep the AER abreast of our findings before the final framework and approach is published.

For CitiPower, Powercor and United Energy, we propose the metric measured by the small scale incentive scheme to be 'customer effort' score. This measures customers' views on how much effort they expend when engaging with our business across the following types of interactions:

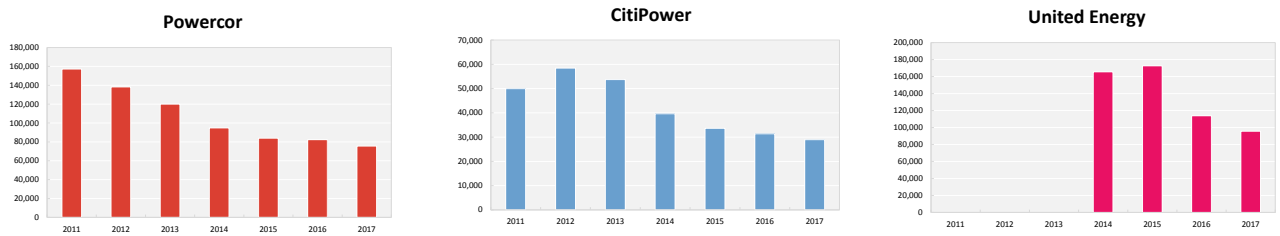
- customer requests
- vegetation management
- unplanned interruptions
- Contact Centre
- public lighting
- planned interruptions.

The scores for each of these interactions are then combined to a single customer effort score measured out of 100%. We propose this measure because it is a fair measure of our customer service and we have a three year history of results for CitiPower and Powercor (and will begin surveys in 2019 for United Energy) for use in setting the targets.

If the small scale incentive is applied, we propose the telephone answering parameter's maximum revenue at risk be halved to 0.25% of revenue. The telephone answering parameter and the small scale incentive scheme incentivise different behaviours—the first incentivise reductions to the time to answer a call, whereas the second incentivises addressing customers' queries in a manner that minimises customers' effort. Nevertheless, there is an interaction between the two because customer effort scores could be improved by answering calls expediently. Therefore in light of this interaction, we would be willing to reduce the telephone answering parameter's revenue at risk.

We also note the number of calls we receive has declined. As shown below, call numbers have approximately halved for CitiPower and Powercor from 2011 when the STPIS applied and for United Energy from 2014 (from when Regulation Information Notice (**RIN**) data is available).

Figure 1 **Number of calls subject to the telephone answering parameter**



Source: RIN data

The decline in call volumes may mean our customer base as a whole could be less willing to pay for improved Contact Centre performance, meaning a halving of the revenue at risk would be appropriate. Nevertheless, the Contact Centre still receives a material number of calls—207 for Powercor, 79 for CitiPower and 262 for United Energy every day of the year on average—and these callers still expect to receive timely service. Therefore it would not be appropriate to remove the telephone answering parameter or adjust the incentive rate.