

APPENDIX 33

2015-20 Cost Allocation Method

Cost Allocation Method

Effective 1 July 2015



Version control

Version	Date of issue	Date of commencement	Description
1.a	February 2009	1 July 2010	AER submitted version – Energex approved
1.b	March 2009	1 July 2010	Minor modifications
2.a	April 2014	1 July 2015	Update following expiry of transitional arrangement in Clause 11.16.3 of the National Electricity Rules on 1 July 2015 and to reflect legal entity and operational structural change

Energex Limited (Energex) commits to retain a listing of the Cost Allocation Method (CAM) and any modifications. Minor updates will be nominated as sub versions of the approved document, e.g. minor style or wording changes that do not alter the meaning will be designated as version 2.b. Substantive changes that amend content or meaning will be given a new version number, e.g. changes to the attribution of costs or the allocation of costs will be designated as version 3.a. Modifications to this document will be in accordance with the National Electricity Rules (NER) and the Cost Allocation Guidelines (“the Guidelines”) requirements.

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Group Manager
Corporate Communications
Energex
GPO Box 1461
BRISBANE QLD 4001

Table of Contents

1	BACKGROUND	1
2	CAM FORMAT AND CONTENTS	2
3	STATEMENT OF NATURE, PURPOSE AND SCOPE OF THE CAM	4
3.1	Nature, purpose and scope of this CAM	4
4	ACCOUNTABILITY FOR IMPLEMENTING THE CAM	5
4.1	Responsibility for updating, maintaining and applying the CAM	5
5	MAINTENANCE OF RECORDS AND VERIFICATION	6
5.1	Work papers	6
5.2	Record retention	6
5.3	Assurance, audit or otherwise verified.....	6
6	CORPORATE AND OPERATIONAL STRUCTURE	7
6.1	Energex company structure	7
6.1.1	Parent entity within the Energex Group.....	8
6.1.2	Operational subsidiary.....	8
6.1.3	Dormant companies	8
6.1.4	Standalone entities	8
6.2	Operational structure	9
6.3	Related parties	10
7	CATEGORIES OF DISTRIBUTION SERVICES.....	11
7.1	Standard control services (SCS).....	13
7.2	Alternative control services (ACS).....	13
7.3	Unclassified services	13
7.4	Other unregulated services	13
7.5	Types of persons to whom distribution services are provided.....	13
8	PRINCIPLES AND POLICIES	15
8.1	Compliance with the Guidelines	15
8.2	Application of principles.....	16
8.3	De-link the CAM from organisational structure	17
8.4	Direct costs	17

8.5	On-cost allocation	19
8.5.1	Labour on-cost.....	19
8.5.2	Materials storage and logistics on-cost	19
8.5.3	Fleet on-cost.....	20
8.6	Indirect cost allocation.....	20
8.6.1	Unregulated cost allocation	22
8.6.2	Regulated overhead rate.....	22
8.7	Allocation of costs to unregulated activities	22
8.7.1	Calculation of the unregulated overhead allocation	23
8.8	Allocation of non-system capex.....	23
9	RECONCILIATION AND CLEARANCE OF POOLS.....	24
9.1	On-cost pool.....	24
9.2	Regulated overhead pool.....	24
9.3	Clearance of under/over recovery.....	24
10	REPLICATING THE CAM.....	25
11	WORK PAPERS	26
12	CAM CONSISTENCY	27
13	MONITORING COMPLIANCE WITH THE CAM AND GUIDELINES.....	28
13.1	Compliance regime.....	28
14	OPERATIONAL DATE OF COMMENCEMENT AND PUBLICATION.....	29
14.1	Date of commencement	29
14.2	Publication and availability of approved CAM.....	29
APPENDIX 1.....		30
Breakdown of Energex indirect costs.....		30
APPENDIX 2.....		31
Cost allocation summary.....		31

1 Background

Energex Limited (Energex) is a Queensland Government Owned Corporation (GOC) that builds, owns, operates and maintains the electricity distribution network in South East Queensland. Energex provides distribution services to 1.3 million connections, delivering electricity to 2.8 million residents and businesses across the region.

Energex's key focus is distributing safe, reliable and affordable electricity in a commercially balanced way that provides value for its customers, manages risk and builds a sustainable future.

As a distribution network service provider (DNSP), Energex is required under clause 6.15.4 of the National Electricity Rules (NER) to submit its Cost Allocation Method (CAM) to the Australian Energy Regulator (AER) for approval. This CAM must give effect to and be consistent with the AER's Cost Allocation Guidelines¹ (the 'Guidelines').

Clause 6.15.4(f) provides that a DNSP may amend its CAM subject to the AER's approval. In order to maintain relevance of the CAM, the following changes have been made and Energex therefore submits this revised CAM for approval:

- Updated the organisational and corporate structure.
- Inclusion of an allocation approach for non-system capital expenditure between service classifications. With the expiry of the transitional rule in clause 11.16.3 of the NER on 30 June 2015, Energex is required to exclude assets, to the extent that they are not used to provide standard control services, from its regulatory asset base (RAB). Previously Energex made a revenue adjustment to account for the alternate use of those assets.
- Minor commentary changes made to ensure wording is consistent throughout the document and improve interpretation of the CAM.

¹ AER Electricity Distribution Network Service Providers, Cost Allocation Guidelines, June 2008.

2 CAM format and contents

Clause 3.2 of the Guidelines sets out the format and contents of a DNSP's CAM. This document complies with clause 3.2 of the Guidelines as follows:

- The version control page sets out information regarding Energex's commitment to recording the version number, history and date of issue for the CAM document (clause 3.2(a)(1) and (2)).
- Section 2 outlines Energex's CAM format and contents summary.
- Section 3 describes:
 - The nature, scope and purpose of Energex's CAM (clause 3.2(a)(3) and 5.1(b)).
 - Energex's commitment to implementing the current version of the CAM (clause 3.2(a)(2)).
- Section 4 articulates:
 - Accountabilities for implementation of the CAM (clause 3.2(a)(3)(A)).
 - Responsibilities within Energex for updating, maintaining and applying the CAM and for monitoring or reporting on its application (clause 3.2(a)(3)(B)).
 - Monitoring of compliance with the CAM and Guidelines (clause 3.2(a)(8)).
- Section 5 describes how Energex will:
 - Maintain work papers and records of the attribution and allocation of costs to, or between, categories of distribution services (clause 3.2(a)(7)).
 - Ensure that allocations and attributions can be verified through assurance, audit or other third party verification process in accordance with clause 5.3 of the Guidelines.
- Section 6 details:
 - Energex's corporate and operational structure which enables delivery of its distribution and other unregulated services (clause 3.2(a)(4)).
 - Related party transactions (clause 3.2(a)(6)).
- Section 7 specifies the categories of distribution services that Energex provides, to which costs are to be attributed or allocated and the types of persons to whom these services are provided (clause 3.2(a)(5)).
- Section 8 outlines the 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 (clause 3.2(a)(6)).
- Section 9 discusses the reconciliation and clearance of on-cost and overhead pools.

- Section 10 outlines the methodology for replicating the CAM outcomes on regulatory accounts.
- Section 11 discusses the structure of Energex's work papers.
- Section 12 considers CAM consistency.
- Section 13 details Energex's monitoring and compliance regime.
- Section 14 provides the operative date for the CAM and its publication details (clause 3.2(a)(9)).

3 Statement of nature, purpose and scope of the CAM

3.1 Nature, purpose and scope of this CAM

Nature: This document represents Energex's revised CAM and has been prepared in accordance with the requirements of Chapter 6 Part F of the NER and the Guidelines. Energex has submitted this CAM to the AER for approval and this revised CAM is to take effect from 1 July 2015.

Purpose: In accordance with Chapter 6 Part F of the NER, this CAM documents the detailed principles and policies used to allocate costs between different categories of distribution services. This CAM gives effect to and is consistent with the cost allocation principles and the Guidelines.

Scope: This document is used by Energex to demonstrate that Energex's CAM gives effect to and is consistent with the Guidelines published by the AER in June 2008. This document sets out the principles and policies for attributing direct costs and the allocation of indirect costs between different categories of electricity distribution services. Energex's Annual Pricing Proposal reflects the required regulated revenue for standard control services, determined based on the application of the CAM and subsequently recovered through tariff charges. For alternative control services, the price of each service reflects the underlying cost, determined based on the application of the CAM.(Refer Figure 7.1).

This CAM is used by Energex in the preparation of capital and operating expenditure forecasts included in Energex's regulatory proposal and regulatory financial reporting to the AER in accordance with the NER.

Energex commits to this CAM and its principles and policies. Any modifications required to this document to ensure its ongoing relevance to the business will be undertaken in accordance with the NER and the Guidelines. Energex will apply the CAM consistently over time.

4 Accountability for implementing the CAM

Accountability for implementing the CAM resides with the Chief Financial Officer.

4.1 Responsibility for updating, maintaining and applying the CAM

The Finance and Strategy & Regulation Divisions have overall responsibility for updating, maintaining and applying the CAM.

- The Group Manager, Regulation & Pricing (Strategy & Regulation Division) is responsible for updating and maintaining the CAM document.
- The Group Manager, Financial Control (Finance Division) is responsible for the application of the CAM in the production of regulatory financial reporting, the monitoring and reporting on the CAM's application and the integration of the CAM into the processes and financial systems used by Energex.

Energex will ensure that accounting records incorporate the application of the CAM and regulatory financial reporting will be based upon these records.

Energex will internally review and monitor application of the CAM for accuracy and completeness. Energex will formally monitor and report on the CAM's application through its internal and external audit programs.

5 Maintenance of records and verification

5.1 Work papers

Energex will maintain all accounting records and ensure they are prepared in accordance with all applicable corporate policies, practices or methods, accounting standards and legislative requirements.

Energex will ensure that accounting records reflect the application of the CAM in the production of regulatory financial reporting.

As part of the annual audit of accounts, supporting work papers are submitted to the auditors for their review. Each work paper is supported by calculations, where appropriate.

5.2 Record retention

In accordance with clause 3.2(a)(7) of the Guidelines, Energex will maintain the following records:

- Whenever financial information is submitted to the AER, work papers will be supplied if requested. The work papers will explain how the numeric quantity or percentage of each allocator has been calculated for each cost item and the source of the data for determining the numeric quantity or percentage.
- Accounting information records will be maintained in accordance with generally accepted accounting practice, Energex policy, applicable taxation requirements, the Corporations Act and any other relevant legislative requirements.
- Source documents, trial balances, transactions listings and cost allocation work papers will be retained in accordance with legislative requirements.

Energex will maintain these records within its integrated financial and assets management systems, such as but not limited to Energex's current general ledger system Ellipse, as well as other specialist application systems and supporting analysis in spreadsheets.

5.3 Assurance, audit or otherwise verified

Audit opinions or other expert opinions will be supplied where required by the NER, to comply with a duly authorised request by the AER, or to comply with appropriate legislation. Auditors' and experts' opinions will be obtained where required and will be requested to be in accordance with standard auditing practice, which includes the application of professional judgement, sampling techniques and materiality.

6 Corporate and operational structure

Energex is a company classified as a GOC under the Government Owned Corporations Act 1993. Energex is owned by the State of Queensland and has two shareholding ministers, the Treasurer and Minister for Trade and the Minister for Energy and Water Supply. The shareholding ministers appoint a Board to provide governance, oversight and strategic direction.

Energex's core business is to supply electricity using its distribution system across South East Queensland.

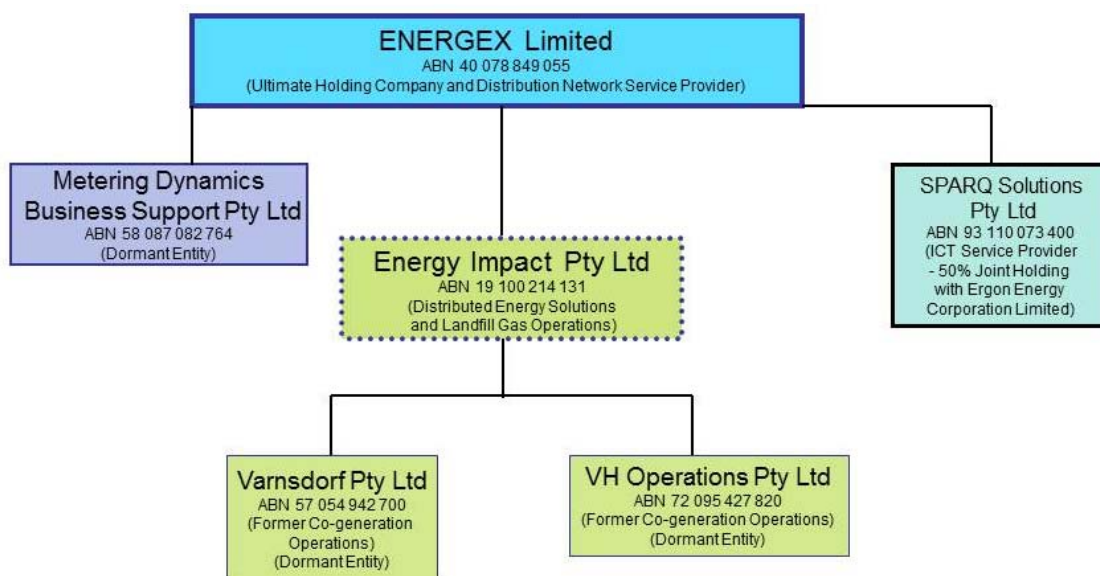
6.1 Energex company structure

Energex is an electricity distribution network business, supplying electricity to a population of approximately 2.8 million people and businesses in South East Queensland. Primarily a network business, Energex also undertakes limited unregulated activities. These unregulated activities include demand side solutions, embedded generation, Type 1- 4 contestable metering, and energy efficiency products.

Unregulated activities are not material in relation to Energex's consolidated financial position, financial performance or total number of employees. Energex's current legal entity structure is shown in Figure 6.1. Some of these entities are dormant and are discussed in Section 6.1.3. This CAM and related working papers refer to Metering Dynamics being an active department within Energex. There is also a dormant company that shares the same name but does not trade.

Energex's legal structure contains a jointly controlled entity that is standalone in that its operations, systems, processes and practices are wholly independent of Energex. This entity does not receive operational support from Energex; hence no shared costs are allocated to this entity. Refer to Section 6.1.4.

Figure 6.1 Energex corporate structure



6.1.1 Parent entity within the Energex Group

The parent entity is Energex Limited ABN 40 078 849 055. Energex Limited is the legal owner of the regulated assets associated with its distribution authority in Queensland and is also the entity that is responsible for the provision of distribution services.

6.1.2 Operational subsidiary

Energy Impact Pty Ltd ABN 19 100 214 131 provides services principally related to embedded generation. The company is also the holding company for two dormant companies in the group.

6.1.3 Dormant companies

Dormant companies are companies that are currently inactive. In the Energex legal structure they include:

- Metering Dynamics Business Support Pty Ltd ABN 58 087 082 764.
- Varnsdorf Pty Ltd ABN 57 054 942 700.
- VH Operations Pty Ltd ABN 72 095 427 820.

6.1.4 Standalone entities

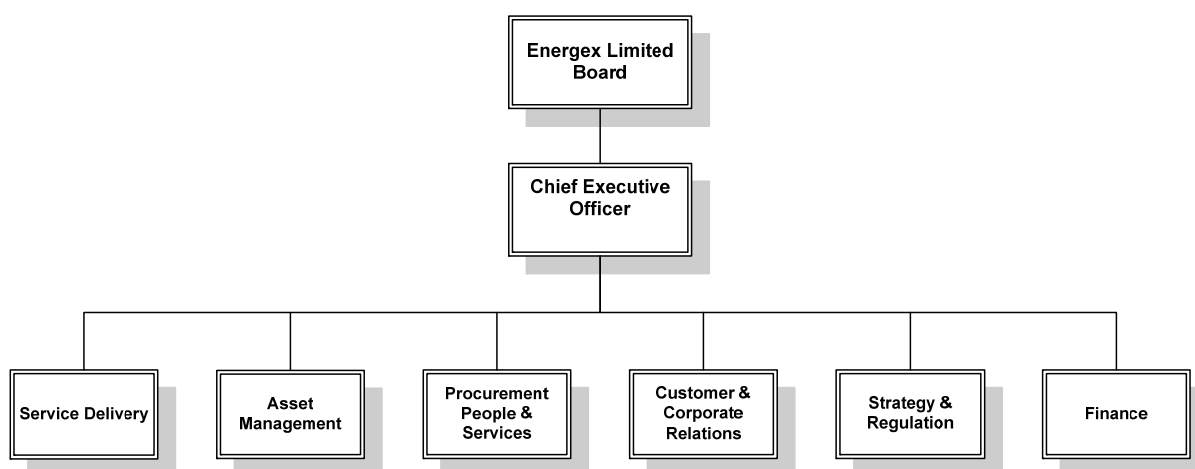
The standalone company is not dependent on Energex for day to day operational, systems, processes and practices, managerial, or strategic assistance. The standalone entity in the Energex legal structure is SPARQ Solutions Pty Ltd ABN 93 110 073 400. The entity is jointly controlled with Ergon Energy and provides information, communication and technology services to both Energex and Ergon.

6.2 Operational structure

Energex is primarily an electricity distribution business. Although Energex also provides limited unregulated activities, these activities are not material² in the context of Energex's overall business operations.

The operating divisions within Energex are Service Delivery; Asset Management; Procurement, People & Services; Customer & Corporate Relations, Strategy & Regulation and Finance. These divisions provide the functions necessary for the establishment and maintenance of the distribution network. Figure 6.2 below sets out Energex's organisational structure.

Figure 6.2: Energex organisational structure



- Service Delivery is focussed on delivering customer needs by safely and efficiently designing, constructing, maintaining and operating the electricity network.
- Asset Management is responsible for network policies, standards, network strategic planning, works program development, safety strategies, environmental management, and network data management.
- Procurement People & Services provide a wide range of targeted support services that facilitate the effective delivery of the Program of Work.
- Customer & Corporate Relations is responsible for Energex customer strategies, management of customer operations and leading two-way interactions between Energex and the customer.
- Strategy & Regulation is responsible for providing strategic direction and economic regulatory oversight to ensure Energex's sustainability in the long term while remaining compliant with regulation.
- Finance provides corporate and financial services that meet our stakeholders' expectations.

² An item is material if its omission, misstatement or non-disclosure has the potential to influence the economic decisions of users taken on the basis of the financial statements or affect the discharge of accountabilities by the management or governing body of the DNSP, gained by an assessment of financial information relating to the DNSP.

6.3 Related parties

As mentioned previously in Section 6.1.4, SPARQ Solutions is a related party. SPARQ Solutions is a company controlled jointly with Ergon Energy that provides information, communication and technology services (ICT) to both companies. Services provided by SPARQ Solutions are:

- service desk services
- desktop services
- communications services
- business application services
- project services, business consulting services and software asset management.

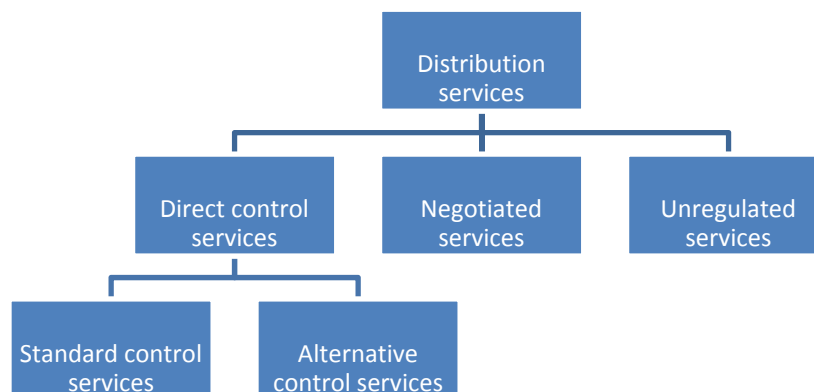
ICT costs incurred by Energex are classified as indirect costs.

Energex does not provide any support services to related parties.

7 Categories of distribution services

The classification of Energex's distribution services are outlined in the AER's final decision on the Framework and Approach paper on Classification of Services and Control Mechanisms³. The distribution service classifications in accordance with the NER are illustrated below in Figure 7.1.

Figure 7.1: Distribution service classifications



Consistent with the requirement to allocate costs to distribution services, this CAM will be used to attribute and allocate costs to the services as approved by the AER.

Energex distribution services are outlined below in Table 7.1.

Table 7.1: Energex distribution services

Distribution service group	Service description	AER service classification
Network services	Planning the network	Standard control service
	Designing the network	Standard control service
	Constructing the network	Standard control service
	Maintaining the network	Standard control service
	Operating the network for DNSP purposes	Standard control service
	Administrative support for the provision of network support	Standard control service

³ AER Final Framework and approach for Energex and Ergon Energy, Regulatory control period commencing 1 July 2015, April 2015.

Distribution service group	Service description	AER service classification
Pre-connection services	General connection enquiry services	Standard control service
	Connection application services	Alternative control service
	Pre-connection consultation services	Alternative control service
Connection services	Small customer connections	Standard control service
	Large customer connections	Alternative control service
	Real estate development connection	Alternative control service
	Removal of network constraint for embedded generator	Alternative control service
	Temporary connections	Alternative control service
Post connection services	Operate and maintain connection assets	Standard control service
	Connection management services	Alternative control service
	Accreditation of alternative control service providers and approval of their designs works and materials	Alternative control service
Metering services	Type 5 and 6 metering installation, provision, maintenance, reading and data services	Alternative control service
	Type 7 metering services	Standard control service
	Auxiliary metering services	Alternative control service
Street lighting services	Provision, construction and maintenance of street lighting	Alternative control service
Ancillary network services	Services provided in relation to retailer of last resort event	Alternative control service
	Other recoverable works	Alternative control service
Unclassified distribution	Type 1-4 metering	Unclassified

Distribution service group	Service description	AER service classification
services	Emergency recoverable works	Unclassified
	Watchman lights	Unclassified
	High load escorts	Unclassified

7.1 Standard control services (SCS)

The NER defines that a standard control service is “a direct control service that is subject to a control mechanism based on a DNSP’s total revenue requirement”⁴. Services are provided to all customers connected to the electricity distribution network.

7.2 Alternative control services (ACS)

The NER states that an alternative control service is a “distribution service that is a direct control service but not a standard control service”⁵. Services are provided to connected customers, third parties, and retailers who request the service.

7.3 Unclassified services

Energex provides distribution services that are unclassified by the AER and therefore are not subject to regulation.

7.4 Other unregulated services

Energex provides a limited range of non-distribution services that are also not subject to regulation.

7.5 Types of persons to whom distribution services are provided

Energex provides distribution services to:

- **Network customers:** Energex provides standard control and alternate control services to over 1.3 million network connected customers in its distribution area. Alternate control services are requested through a retailer or in some circumstances can be requested directly by the customer.
- **Third party customers:** Energex provides alternate control services to third parties (e.g. local council, real estate developers).

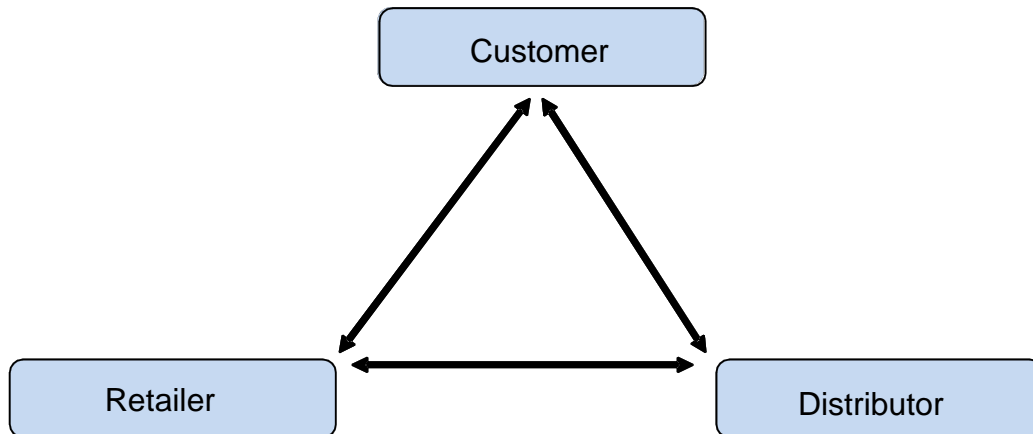
⁴ National Electricity Rules Chapter 10

⁵ National Electricity Rules Chapter 10

- **Electricity retailers:** Retailers purchase wholesale energy that is transported through Powerlink's transmission system, and Energex's distribution system, to network connected customers. Retailers also request alternate control services (e.g. disconnection, special meter read) on behalf of customers.

A tripartite relationship between Energex, customers and retailers exists which is illustrated in Figure 7.2:

Figure 7.2: Tripartite relationship



Energex provides connection services to customers under either a Standard or Negotiated Connection Contract. With the proposed introduction of NECF on 1 July 2015, the current standard connection contract will be replaced with the deemed standard connection contract under the National Energy Retail Rules, which is consistent with the current contract. Similarly, the interaction with retailers will be managed through the application of Chapter 6B of the National Electricity Rules.

8 Principles and policies

8.1 Compliance with the Guidelines

In accordance with clause 2.2.5 of the Guidelines Energex commits to the following principles:

- Not to allocate the same cost more than once.
- A direct cost will only be allocated to one category of distribution service.
- An indirect cost will only be allocated once between categories of distribution services.
- The same cost will not be treated as both a direct and an indirect cost.
- Energex will recover the same cost only once through the charges for its distribution services.

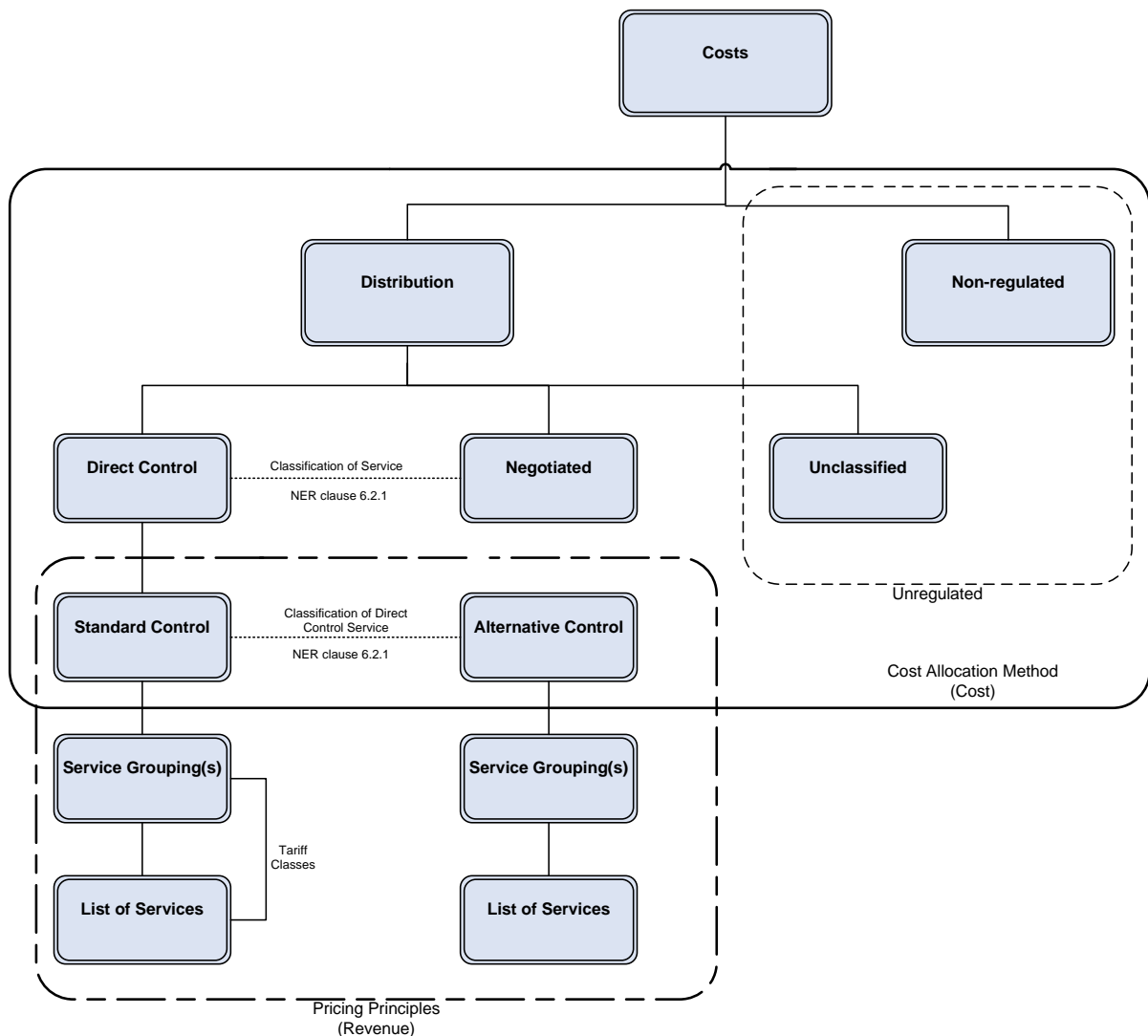
In accordance with the requirements of clause 2.2.2 of the Guidelines Energex confirms that the application of this CAM will facilitate the attribution of costs directly to, or allocate costs between categories of distribution services on the substance of the underlying transaction or event, rather than the legal form, where they differ. In addition Energex:

- Will not allocate indirect costs using an avoided cost approach without prior approval by the AER (clause 2.2.4(e)).
- Confirms the compliance of this CAM with the distribution ring-fencing obligations (clause 2.2.6).
- Acknowledges that costs that have been allocated to a service will not be reallocated to another service during the course of a regulatory period (clause 2.2.7).

Energex's CAM will employ the principles outlined above to attribute or allocate costs to distribution services as defined in the Guidelines. Figure 8.1 represents a conceptual outline of the CAM as it applies to the various services outlined in Section 7. Further, it defines the point of interface between the CAM and Energex's pricing methodology. Figure 8.1 demonstrates graphically how the CAM will interact with the Pricing Principles to attribute and allocate costs to distribution services.

This CAM does not include an avoided cost allocation approach.

Figure 8.1: Conceptual model of interface to pricing model



8.2 Application of principles

Energex applies the above principles in the following manner:

- **Attribution of direct costs:** Opex and/or capex to distribution services and/or unregulated activities where causation supports attribution as outlined in Section 8.4.
- **Allocation of on-costs:** On-costs for labour, materials storage and logistics and fleet for direct opex and/or direct capex as outlined in Section 8.5.
- **Allocation of regulated overheads:** These costs will be allocated to distribution services as a proportion of total opex and capex direct spend on the service.
- **Allocation to unregulated activities:** A portion of indirect costs will be allocated to unregulated activities as outlined in Section 8.7.

- **Allocation of non-system capex:** An allocation of capex to non-standard control services (i.e. alternative control, unregulated) is undertaken where appropriate to reflect their use in delivery of those services and is outlined in Section 8.8.

The guiding principles of Energex's CAM ensure that costs consumed by each activity or service are reflected appropriately and more specifically that the costs attributable to unregulated activities are segregated from the regulated activities.

A summary outlining the basis of costing for each of the above principles can be found in Appendix 2.

8.3 De-link the CAM from organisational structure

Energex is principally a DNSP and the vast majority of Energex's costs relate solely to the distribution business. Therefore, this CAM will be used to consistently map costs to distribution services independent from the organisational structure in compliance with cost allocation principles and objectives within the Guidelines and the NER.

Energex's CAM focuses on attributing costs to activities which are mapped directly to a distribution service. This enables Energex to apply its CAM independent from its organisational structure.

8.4 Direct costs

A direct cost is an expenditure item that is directly attributable, via a source document, to the provision of distribution services. Direct costs are attributed to activities which are mapped to associated services. Direct costs are therefore directly attributed by a source document to each of the service classifications as outlined in Section 7 of this CAM.

On-costs associated with direct costs will be attributed directly to each service based on the proportion of direct costs incurred by that service. On-costs are discussed in more detail in Section 8.5 below.

The nature of direct costs and associated on-costs for Energex include:

- labour and labour related costs
- contractor costs
- materials, storage and logistics costs
- fleet.

All of Energex's services incur direct costs. Direct costs are primarily attributed directly to the relevant service via work orders, invoices and journal entries in the general ledger system. The direct cost is booked by cost element (i.e. labour, material or contractor) to an account code which is specific to an individual service within a service classification. Table 8.1 below provides further details on the allocation of direct costs.

Table 8.1: Attribution of Energex direct costs and allocation of associated on-costs

Nature of Cost	Description	Attributed to	Basis of Costing
Labour and labour related costs: directly incurred in the provision of distribution services	Salaries, wages and other employee related on-costs (superannuation, payroll tax, workers compensation, annual and long service etc)	Standard control services Alternative control services Unregulated activities	Directly attributed based on timesheets ultimately linked to service specific account codes. The payroll related costs (labour on-costs) are charged as part of the standard labour rate.
Contractor costs: directly incurred in the provision of distribution services	Payments to contractors for their services	Standard control services Alternative control services Unregulated activities	Directly attributed to account code based on source documents.
Materials and materials related costs: directly incurred in the provision of distribution services	Material costs, including an associated charge to cover the on-costs of administration, warehousing and logistics	Standard control services Alternative control services Unregulated activities	Materials are directly attributed to account code based on source documents. The logistics and warehousing related costs (materials and logistics on-costs) are charged as a standard rate on direct materials issued to each service.
Fleet charges: directly incurred in the provision of distribution services	Motor vehicle leasing and fleet operating, management and administration costs; including other costs such as registration and fuel	Standard control services Alternative control services Unregulated activities	Fleet on-cost is charged as a standard rate, based on direct labour spend in each service.
Journals	Manual adjustments	Standard control services Alternative control services Unregulated activities	Specific attribution based on nature of adjustment.

Direct attribution via work orders and invoices takes place in the Energex general ledger system. Work orders, invoices and the ledger have a clear audit trail.

8.5 On-cost allocation

On-costs are expenditure items that are not directly attributable to a service via source document, but arise as a consequence of incurring direct attributable costs. Therefore the expenditure categorised as on-costs are added to direct expenditure that has been attributed to services.

Energex has three specific types of on-costs:

- labour on-costs
- materials storage and logistics on-costs
- fleet on-costs.

As detailed in the previous section direct costs are attributed to services via source documents (e.g. work orders and/or invoices). On-costs are attached to the relevant direct expenditure and are therefore allocated on the basis of that direct spend. For example, materials storage and logistics on-cost is attached to each dollar of direct materials expenditure issued from store and attributed to a service on this basis.

Each on-cost rate is calculated at the beginning of the year based on budgeted expenditure. The method for calculating each rate is discussed below. The process for reviewing and reconciling the on-cost rates is outlined in Section 9.

8.5.1 Labour on-cost

Labour on-cost comprises expenditure associated with the following items:

- payroll tax
- superannuation
- other employee costs (e.g. leave provisions).

Labour on-cost will be calculated as follows:

$$\frac{\textit{Total labour expenditure on-costs (\$)}}{\textit{Total wages and salaries expenditure (\$ spend)}}$$

These costs are on-costed (added on) to basic employee wages and salaries as this reflects the true labour cost.

8.5.2 Materials storage and logistics on-cost

Materials storage and logistics on-cost reflects expenditure incurred to store, coordinate and issue physical items that are attributable as direct materials expenditure. This expenditure is primarily materials handling and storage costs associated with operating this function.

Materials storage and logistics on-cost charge will be calculated as:

$$\frac{\text{Total materials storage \& logistics expenditure on-costs (\$)}}{\text{Total direct materials expenditure (\$ spend)}}$$

Materials stores and logistics on-cost charge will be attached to direct material expenditure, in accordance with the above ratio, to reflect the true cost associated with the consumption of material components.

8.5.3 Fleet on-cost

The fleet on-cost comprises expenditure incurred to operate and maintain vehicles owned or leased by Energex that are used in the construction, operation and maintenance of the electricity network. These costs include items such as:

- employee costs (for staff involved in fleet operations)
- fuel and oil
- vehicle maintenance
- registration and insurance
- other similar types of fleet costs.

Fleet on-cost charge will be calculated as:

$$\frac{\text{Total fleet expenditure on-costs (\$)}}{\text{Total direct labour expenditure (\$ spend)}}$$

This expenditure is attached to direct labour expenditure associated with delivery of services on the basis that wherever direct labour is utilised, fleet would have been required to transport employees and their equipment. There is a strong correlation between labour effort and fleet consumption. Consequently, fleet charges are attached to direct labour (inclusive of the labour on-cost).

8.6 Indirect cost allocation

Indirect costs are costs that are necessarily incurred in the provision of services, but are not directly attributed by a work order or invoice to a specific activity or service. Indirect costs in Energex's context include costs that support distribution and unregulated services and are allocated to services as appropriate. These costs include:

- Materials and fleet on-costs which are allocated as detailed above in Sections 8.5.2 and 8.5.3 and are excluded from regulated overhead costs.
- Unregulated support costs, which are allocated to unregulated activities as detailed in sections 8.6.1 and 8.7 below and are excluded from regulated overhead costs.

- Other operating costs which are regulated support costs that are excluded from the regulated overhead costs and represents costs not allocated to individual services but remain as regulated operating expenditure. These costs relate to the following functions:
 - Audit
 - Finance
 - Legal and Secretariat
 - Strategy, Regulation and Stakeholder engagement
 - Human Resources
- Regulated overhead costs are the remaining indirect costs allocated to regulated services on the basis of total direct spend for each service. Refer to Appendix 1.

Regulated overhead costs include the following functions:

- Information, Communication and Technology
- Occupancy and facility management
- Network planning and project governance
- Resource management
- Field and business support
- Training and development
- Organisation health and safety

Costs associated with these functions would only be classified as indirect to the extent that they cannot be directly attributed to a service.

A causal relationship cannot always be easily established for the allocation of indirect costs. However, these costs are necessarily incurred as a result of the services provided by Energex.

Energex has determined that regulated overheads are allocated to regulated services on the basis of total direct spend as this reflects a strong correlation with the consumption of the overhead.

The regulated overhead rate and the unregulated allocation rate are calculated at the beginning of the year based on budgeted expenditure. The method for calculating each rate is discussed below. The process for reviewing and reconciling the regulated overhead rate is outlined in Section 9.

8.6.1 Unregulated cost allocation

The unregulated cost allocation is based on the allocation process described in Section 8.7 and is allocated to unregulated activities prior to determining the regulated overhead rate. The allocation is determined after taking into account the size, scale and scope of the unregulated activities compared to the total Energex business.

8.6.2 Regulated overhead rate

The regulated overhead rate reflects the remaining indirect expenditure related to Energex's regulated services. The regulated overhead pool is determined on the basis of the total indirect costs after deducting the specific items listed in Section 8.6 above.

The regulated overhead rate will be determined by the size of the pool divided by the direct operating and capital expenditure (including contractor spend, labour spend and material spend inclusive of on-costs) of the regulated distribution services.

The rate is calculated as follows:

$$\frac{\text{Total regulated overheads (\$)}}{\text{Total direct expenditure (opex and capex \$ spend)}}$$

8.7 Allocation of costs to unregulated activities

In addition to its regulated distribution services, Energex also conducts unclassified distribution services and other unregulated activities. As mentioned in Section 8.2 direct costs (capex and opex) are allocated to unregulated activities on a causation basis.

Energex has documented the services and determined that the most appropriate basis for overhead cost allocation to unregulated activities is by a three factor method based on assets, headcount and revenue. Utilising the three factor method allows consideration to be taken of the materiality, scale and size of the unregulated activities in comparison to the regulated activities.

The three factor method will be applied to each year's budget to determine the appropriate cost allocation for that year. This will ensure that the allocation is current and reflects changes in size, scale and scope of the unregulated activities.

The three factor process will include a review requirement linked to a material change in size, scale and scope of the unregulated activities or a material increment or decrement in the services provided to adjust the allocation accordingly.

The allocation of indirect costs to the unregulated activities will be deducted from the total remaining indirect costs, ensuring that indirect costs are only allocated once.

8.7.1 Calculation of the unregulated overhead allocation

The unregulated overhead allocation is calculated via the three factor method as detailed below.

Factor 1: Asset % is calculated as follows:

$$\frac{\text{Total unregulated assets}}{\text{Total regulated and unregulated assets}}$$

Factor 2: Headcount % is calculated as follows:

$$\frac{\text{Total unregulated headcount}}{\text{Total regulated and unregulated headcount}}$$

Factor 3: Revenue % is calculated as follows:

$$\frac{\text{Total unregulated revenue (excl. interest revenue)}}{\text{Total regulated and unregulated revenue (excl. interest revenue)}}$$

The average of the three percentages forms the percentage of indirect costs to be allocated to the unregulated services.

8.8 Allocation of non-system capex

Where appropriate, assets are directly allocated to their relevant service classifications at time of purchase or construction, however a range of non-system assets are used to alternately provide SCS, ACS and unregulated services. While the majority of these assets are used in the provision of SCS, some are used to deliver a range of services in other service classifications. Throughout the 2010-2015 regulatory period Energex relied on the transitional arrangement in clause 11.16.3 of the NER to limit the need to allocate these assets and associated capital expenditure between the RAB and other service classification bases. However, with the expiry of this transitional provision on 30 June 2015, Energex will standardise the allocation basis for capital expenditure on non-system assets used to deliver multiple services.

Energex's non-system assets include:

- non-system property (e.g. land and buildings)
- fleet
- tools and equipment
- minor ICT assets (e.g. end user devices).

Energex will allocate non-system capital expenditure to service classifications based on causal drivers representing the most appropriate utilisation of the underlying assets. Predominantly non-system capital expenditure would be allocated based on the proportion of labour incurred in delivering services within each classification. Employee usage represents the most indicative underlying driver for the purchase, construction and use of the above non-system assets. The drivers will be reviewed annually to ensure continuing relevance to the utilisation of the asset.

9 Reconciliation and clearance of pools

All on-cost and overhead rates are established at the beginning of the financial year. The rates are based on budget data and each represents the expected consumption of that pool of costs. As the year progresses a process tracks the rates to actual expenditure and they are adjusted where necessary. This process is discussed below.

9.1 On-cost pool

Each on-cost rate is calculated at the beginning of the year based on budget expenditure. The method for calculating each rate is discussed above in Section 8.5. The rates are applied to actual direct expenditure throughout the year. On a quarterly basis the budget rate is reviewed against actual expenditure. Where there are material variances an adjustment is made to the rate, however the methodology applied is consistent.

9.2 Regulated overhead pool

As stated above, this rate is based on budget data. The method for calculating the rate is discussed above in Section 8.6.2. The rate is applied to actual direct expenditure throughout the year. On a quarterly basis the forecast rate is reviewed against actual expenditure. Where there are material variances an adjustment is made to the rate, however the methodology applied is consistent.

9.3 Clearance of under/over recovery

A surplus or deficit in the on-cost or overhead pools is cleared to a central pool. This pool is cleared via an allocation across the services based on direct spend.

For material variances a review is carried out to determine the most appropriate treatment for each over or under recovery.

10 Replicating the CAM

The purpose of this chapter is to fulfil Clause 2.2.1(b)(1)(B) of the Guidelines which requires that a DNSP include information to the extent necessary to enable the AER to replicate its reported outcomes.

The AER will be able to replicate the outcomes of the CAM utilising Energex's responses to Regulatory Information Notices, supplemented by the work papers referred to in Section 11.

11 Work papers

Applying, reconciling and auditing the CAM at an operational level within the business requires detailed work papers. The work papers provide detailed information specific to Energex's various systems and general ledger. This information is required at an operational level to ensure the high level outcomes and principles of the CAM are achieved.

The work papers include items such as:

- Specific expenditure items that relate to direct costs.
- Specific expenditure items that form each on-cost pool.
- Specific expenditure items that form the regulated overhead pool.
- The calculation of the unregulated allocation.
- The basis of allocation of each on-cost and overhead pool.
- The calculation method for each on-cost rate.
- The calculation of the regulated overhead rate.
- The calculation of the allocator for non-system assets.
- The clearance of any over or under recovery of on-costs or regulated overheads.

12 CAM consistency

Policies and principles relating to allocations will be consistently applied across accounting periods to ensure that regulatory financial reports are prepared on a consistent basis over time.

Energex will apply the CAM consistently each year. As the nature of costs may change from time to time, Energex will periodically review the CAM and make appropriate changes to ensure that its application results in:

- Consistency with prior accounting and regulatory periods.
- The basis of cost attribution or cost allocation being considered on the substance of the transaction over its legal form.

13 Monitoring compliance with the CAM and Guidelines

The Finance Division is responsible for monitoring and ensuring compliance with the CAM across Energex. Operationally, the Group Manager Financial Control will be responsible on a day to day basis for compliance.

13.1 Compliance regime

Energex's annual statutory financial statements and the system that captures financial information and is used as the source of the statements (Ellipse) are reviewed by our external auditor, the Queensland Audit Office.

Energex will undertake, as directed by the AER, an independent audit of its regulatory financial reports to ensure they are compliant with regulatory reporting requirements, including the CAM.

Energex can also independently monitor and report on the CAM's application through internal and external audit programs that are in addition to those specified above. This includes scheduled or ad hoc audit programs of specific areas identified by either management or owners.

14 Operational date of commencement and publication

14.1 Date of commencement

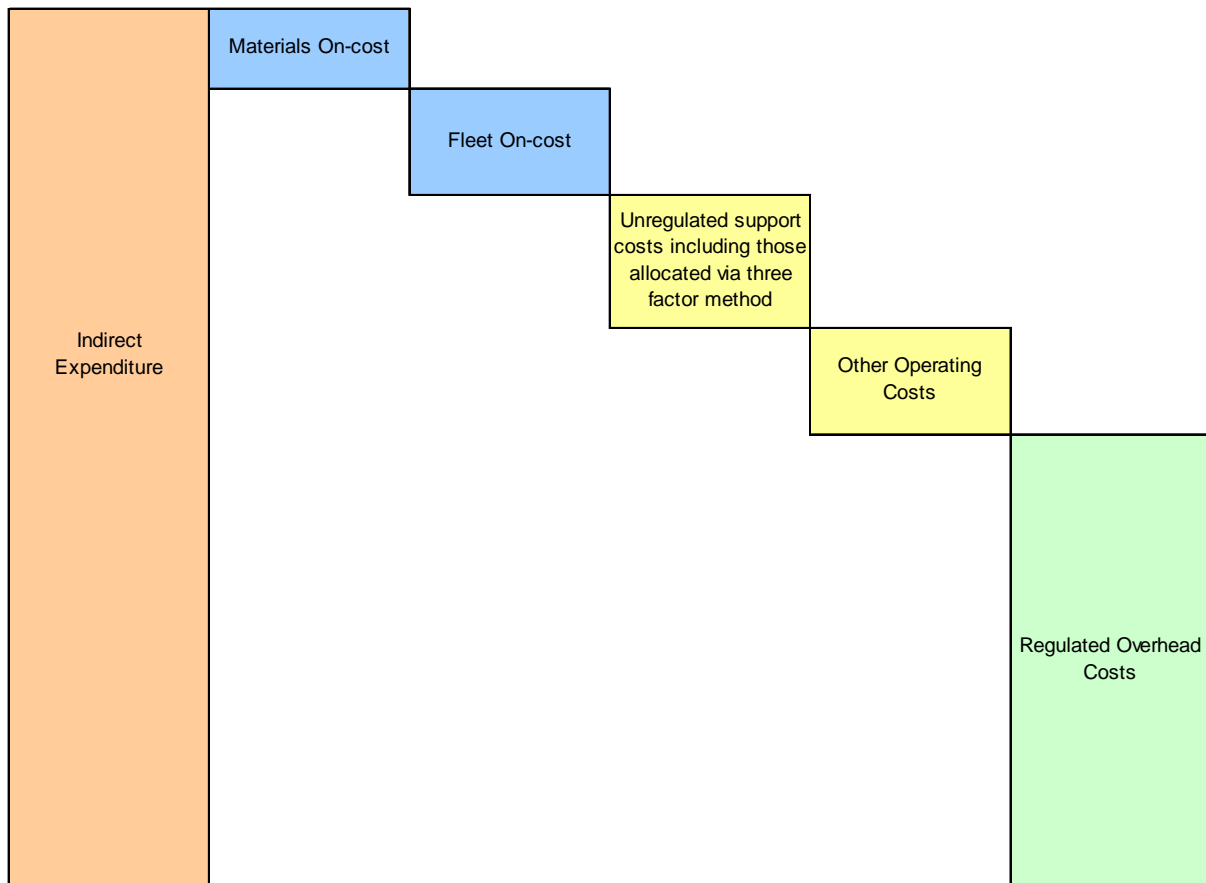
This CAM is effective from the start of the regulatory period commencing on 1 July 2015 and will remain in force until such time as a new or amended CAM is approved by the AER in accordance with the NER and the Guidelines.

14.2 Publication and availability of approved CAM

In accordance with the requirements of clause 6.15.4(h) of the NER, Energex will maintain a copy of its approved CAM on its website, www.energex.com.au. Further, Energex will supply the AER with an electronic version (in PDF form) and printed copies if required.

Appendix 1

Breakdown of Energex indirect costs



Appendix 2

Cost allocation summary

Table A2.1: Allocation of Energex costs

Nature of cost	Description	Attributed/Allocated to	Basis of costing
Direct expenditure	Expenditure that is directly attributable to the provision of distribution services	Standard control services Alternative control services Unregulated services	Attributed via source document
Labour on-cost	Expenditure associated with payroll tax, superannuation and other employee costs	Standard control services Alternative control services Unregulated services	Allocated based on total direct wages and salary expenditure
Materials storage and logistics on-costs	Expenditure associated with materials handling and storage costs	Standard control services Alternative control services Unregulated services	Allocated based on total direct materials expenditure
Fleet on-costs	Expenditure associated with operating and maintaining motor vehicles (owned and leased)	Standard control services Alternative control services Unregulated services	Allocated based on direct labour
Indirect cost allocation to unregulated (unregulated cost allocation)	Corporate support expenditure incurred in supporting the provision of unregulated services but not directly attributed to specific unregulated activity or service	Unregulated services	Allocated based on the three factor method which includes: assets; head count and revenue
Indirect cost allocation (incl. regulated overhead)	Expenditure incurred in the provision of services but not directly attributed to specific activity or service	Standard control services Alternative control services	Regulated overhead allocated based on total direct expenditure (OPEX and CAPEX)

Nature of cost	Description	Attributed/Allocated to	Basis of costing
Non System CAPEX	Allocation of CAPEX used to deliver ACS & unregulated services	Standard control services Alternative control services Unregulated services	Allocated based on causal relationship (e.g. labour)