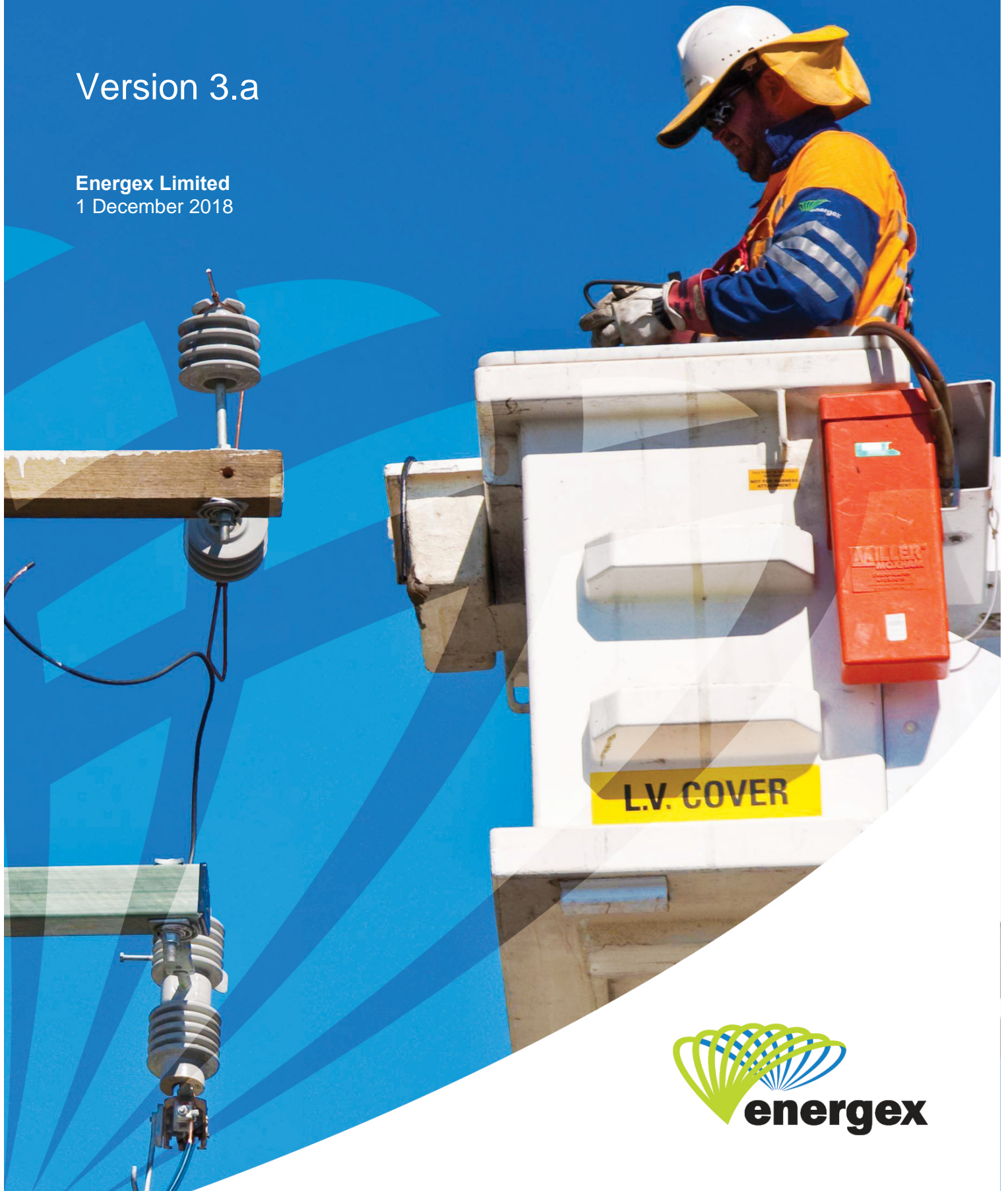


Energex Cost Allocation Method

Version 3.a

Energex Limited
1 December 2018



Version Control

Version	Date	Description
1.a	February 2009	AER submitted version – Energex approved
1.b	March 2009	Minor modifications
2.a	April 2014	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.
3.a	July 2018	Updated to reflect changes in corporate and organisational structure, accountability for the CAM, and modifications to the document format.

Section 3.2(a)(2) of the Australian Energy Regulator's Cost Allocation Guidelines¹ requires that this Cost Allocation Method include the Distribution Network Service Provider's commitment to history and date of issue for the document. This is detailed in the table below. 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 1.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 2.b. Modifications of this document will be in accordance with the National Electricity Rules (NER) and the Cost Allocation Guidelines requirements.

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¹ Electricity distribution network service providers, Cost allocation guidelines, June 2008

Contents

1	BACKGROUND	1
2	CAM FORMAT AND CONTENTS	1
3	NATURE, SCOPE AND PURPOSE OF CAM	3
	3.1 Nature	3
	3.2 Purpose	3
	3.3 Scope.....	3
4	DATE OF COMMENCEMENT	4
5	ACCOUNTABILITY FOR THE CAM.....	4
6	CORPORATE STRUCTURE	5
7	OPERATIONAL STRUCTURE	7
8	CATEGORIES OF DISTRIBUTION SERVICES	9
	8.1 Standard control services (SCS)	9
	8.2 Alternative control services (ACS).....	9
	8.3 Unclassified services	9
	8.4 Other unregulated services	9
	8.5 Negotiated services.....	10
	8.6 Types of persons to whom distribution services are provided	11
9	COST ALLOCATION PRINCIPLES & POLICIES	12
	9.1 Compliance with the Guidelines.....	12
	9.2 Application of principles.....	14
	9.3 De-link the CAM from organisational structure.....	14
	9.4 Direct costs	14
	9.5 On-cost allocation	16
	9.5.1 Labour on-cost	16
	9.5.2 Materials storage and logistics on-costs.....	16
	9.5.3 Fleet on-costs	17
	9.6 Indirect cost allocation.....	17
	9.6.1 Unregulated cost allocation	18
	9.6.2 Regulated overhead rate.....	18
	9.7 Allocation of costs to unregulated activities.....	18
	9.7.1 Calculation of the unregulated overhead allocation.....	19
	9.8 Allocation of non-system capex.....	19

10	RECONCILIATION AND CLEARANCE OF POOLS.....	20
	10.1 On-cost pool	20
	10.2 Regulated overhead pool.....	20
	10.3 Clearance of under/over recovery.....	20
11	REPLICATING THE CAM.....	21
12	WORK PAPERS	21
13	CAM CONSISTENCY	21
14	RECORD KEEPING.....	21
15	MONITORING COMPLIANCE WITH THE CAM AND CAG.....	22
16	APPENDIX A: BREAKDOWN OF ENERGEX INDIRECT COSTS	23
17	APPENDIX B: COST ALLOCATION SUMMARY	24
18	APPENDIX C: COMPLIANCE WITH CAG, RFG and NER	25

1 BACKGROUND

Clause 6.15.4(f) of the National Electricity Rules (NER) provides that a DNSP may amend its Cost Allocation Method (CAM) subject to the Australian Energy Regulators (AER's) approval. In order to maintain relevance of the CAM, the following changes have been made to Energex Limited's (Energex's) CAM:

- Update the organisational and corporate structure to reflect the integration of Energex under a common parent entity, Energy Queensland Limited (EQL) and operating model;
- Ensure consistency and demonstrate compliance with the AER's Ring-Fencing Guidelines (RFG);
- Minor changes made to update or clarify issues to improve interpretation.

2 CAM FORMAT AND CONTENTS

Clause 3.2 of the CAG sets out the format and contents of a DNSP's CAM. This document complies with clause 3.2 of the CAG 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 1](#) provides the background to the CAM amendment;
- [Section 2](#) outlines the CAM format and contents summary;
- [Section 3](#) describes the nature, scope and purpose of Energex's CAM (clause 3.2(a)(3));
- [Section 4](#) provides the operative date for the CAM (clause 3.2(a)(9));
- [Section 5](#) outlines the accountability for implementing the CAM (clause 3.2(a)(3)(A)) and responsibilities for updating, maintaining and applying the CAM and for internally monitoring or reporting on its application (clause 3.2(a)(3)(B)) across Energex's Distribution Network;
- [Section 6](#) presents Energex's Corporate Structure, identifying the relationships between the distribution networks and the broader Energy Queensland Group (clause 3.2(a)(4));
- [Section 7](#) presents the operating structure of Energex's network under the common Energy Queensland Group management team (clause 3.2(a)(4));
- [Section 8](#) describes the categories of distribution services that are provided by the Energex's network and describes the parties that these services are provided to (clause 3.2(a)(5));
- [Section 9](#) summarises the Cost Allocation Principles and Policies that are applied in accordance with the CAG and RFG and provides an overview of the financial systems that are used to implement and report against the CAM and describes how capital expenditure, shared assets and shared costs are treated (clause 3.2(a)(6));
- [Section 10](#) discusses the reconciliation and clearance of on-cost and overhead pools;
- [Section 11](#) outlines the methodology for replicating the CAM outcomes on regulatory accounts;
- [Section 12](#) discusses the structure of Energex's work papers (clause 3.2(a)(7));
- [Section 13](#) considers CAM consistency;
- [Section 14](#) details Energex's monitoring and compliance regime (clause 3.2(a)(8));
- [Appendix A](#) summarises the breakdown of Energex's indirect costs;
- [Appendix B](#) summarises the basis of costing that attributes or allocates costs to services by the nature of the cost.; and

- [Appendix C](#) provides a compliance checklist against the requirements of the CAG, RFG, and NER.

3 NATURE, SCOPE AND PURPOSE OF CAM

3.1 Nature

This CAM document has been prepared in accordance with the requirements of Chapter 6 Part F of the NER and the CAG. Energex has submitted this CAM to the AER for approval to take effect from 1 July 2018, superseding the current CAM document for Energex [version 2.a].

3.2 Purpose

This document sets out the principles and policies for attributing direct costs and the allocation of indirect costs between different categories of distribution services, that is, between direct control services (standard control services and alternative control services) and unregulated distribution services.

The method and principles established in this document are also applied to attribute and allocate costs to non-distribution services, ensuring that only those costs associated with Energex's distribution services are then attributed to or allocated between the categories of distribution services.

3.3 Scope

This CAM gives effect to and is consistent with the cost allocation principles and the CAG. Specifically:

- The CAM attributes costs directly to, or allocates costs between, categories of Distribution Services on the substance of the underlying transaction or event, rather than the legal form, as required by section 2.2.2 of the CAG;
- Only costs that are directly attributable to the provision of a particular category of Distribution Services are directly attributed to those services, as required by section 2.2.3 of the CAG;
- The CAM allocates shared costs between categories of Distribution Services using appropriate causal allocators, as required by section 2.2.4 of the CAG;
- The CAM does not allocate the same cost more than once, as required by section 2.2.5 of the CAG;
- The detailed principles, policies and approach used to attribute costs directly to, or allocate costs between, categories of Distribution Services are consistent with the applicable Ring-Fencing Guidelines under clause 6.17 of the Rules, as required by section 2.2.6 of the CAG; and
- Energex will not reattribute or reallocate costs from a Distribution Service to another service during the course of a regulatory control period, as required by section 2.2.7 of the CAG.

Energex will apply this CAM to prepare:

- Prices for a Negotiated Distribution Service determined in accordance with clause 6.7.1 of the Rules;
- Annual statements in accordance with any regulatory information instruments; and

- Actual or estimated capital expenditure for the purposes of adjusting the value of Energex's regulatory asset base under Schedule 6.2.1(f) of the Rules.

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

4 DATE OF COMMENCEMENT

This CAM is effective from the 1 December 2018 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 CAG. Upon its commencement, this CAM will supersede all earlier versions.

5 ACCOUNTABILITY FOR THE CAM

Accountability for implementing the CAM resides with the Chief Financial Officer (CFO) through the finance and regulatory functions within EQL.

The day-to-day responsibility for the CAM is shared between the:

- Group Manager Financial Control, who 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.
- General Manager Regulation and Pricing who is responsible for monitoring compliance of the CAM with the NER and the CAG.

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 the application of the CAM for accuracy and completeness. This includes formally monitoring and reporting on the CAM's application through its internal and external audit programs.

6 CORPORATE STRUCTURE

Section 3.2(a)(4) of the CAG requires the CAM to include a description of the DNSP's corporate structure.

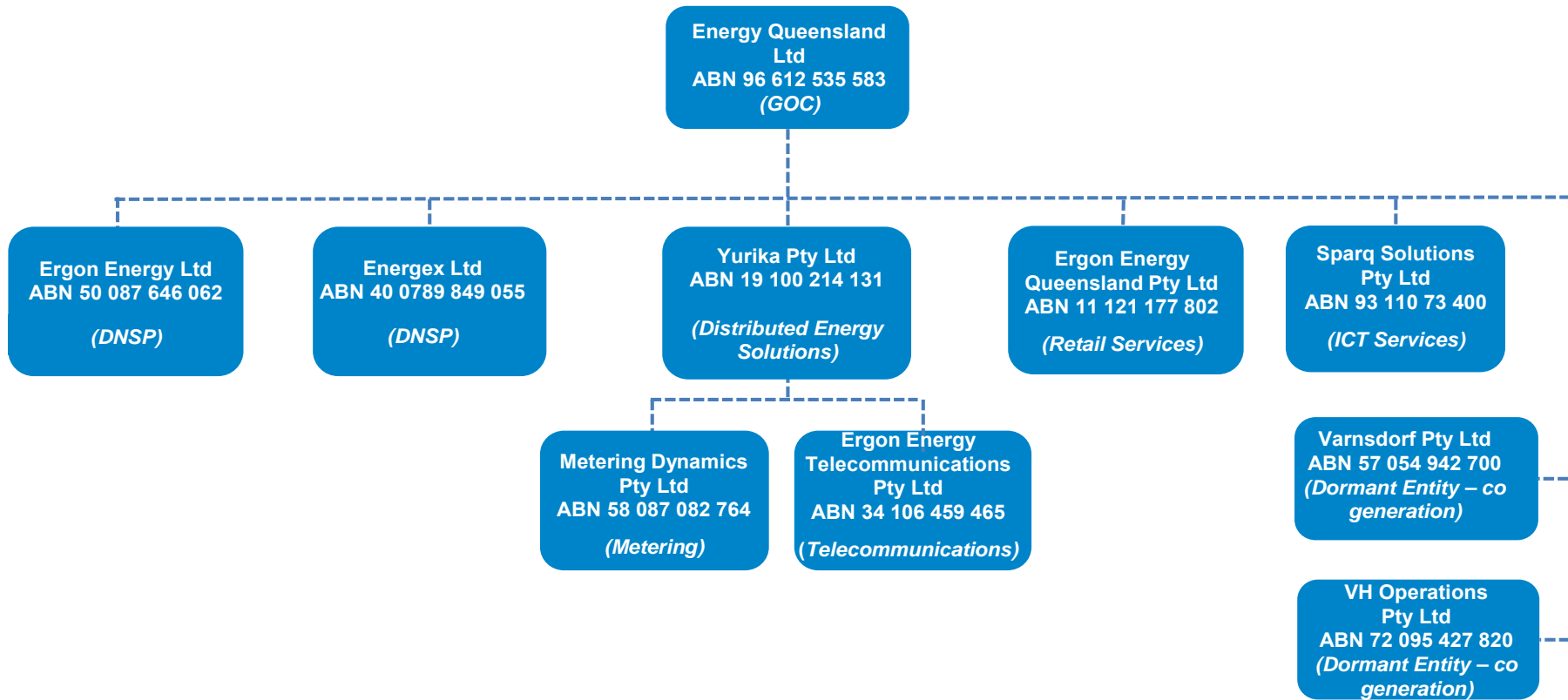
Energex is a wholly owned subsidiary of EQL. EQL, which commenced operations on 30 June 2016, is a Queensland Government Owned Corporation (GOC) that is the holding company for Energex.

Energex is an electricity distribution network business, supplying electricity to a population of approximately 2.8 million people and businesses 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.

The corporate structure for Energex is shown in Figure 1 below.

Figure 1: Energex's Corporate Structure in the EQL Group



7 OPERATIONAL STRUCTURE

Energex operates under a common management team and delivers services through functional units shown in Figure 2 below. The integrated operational structure:

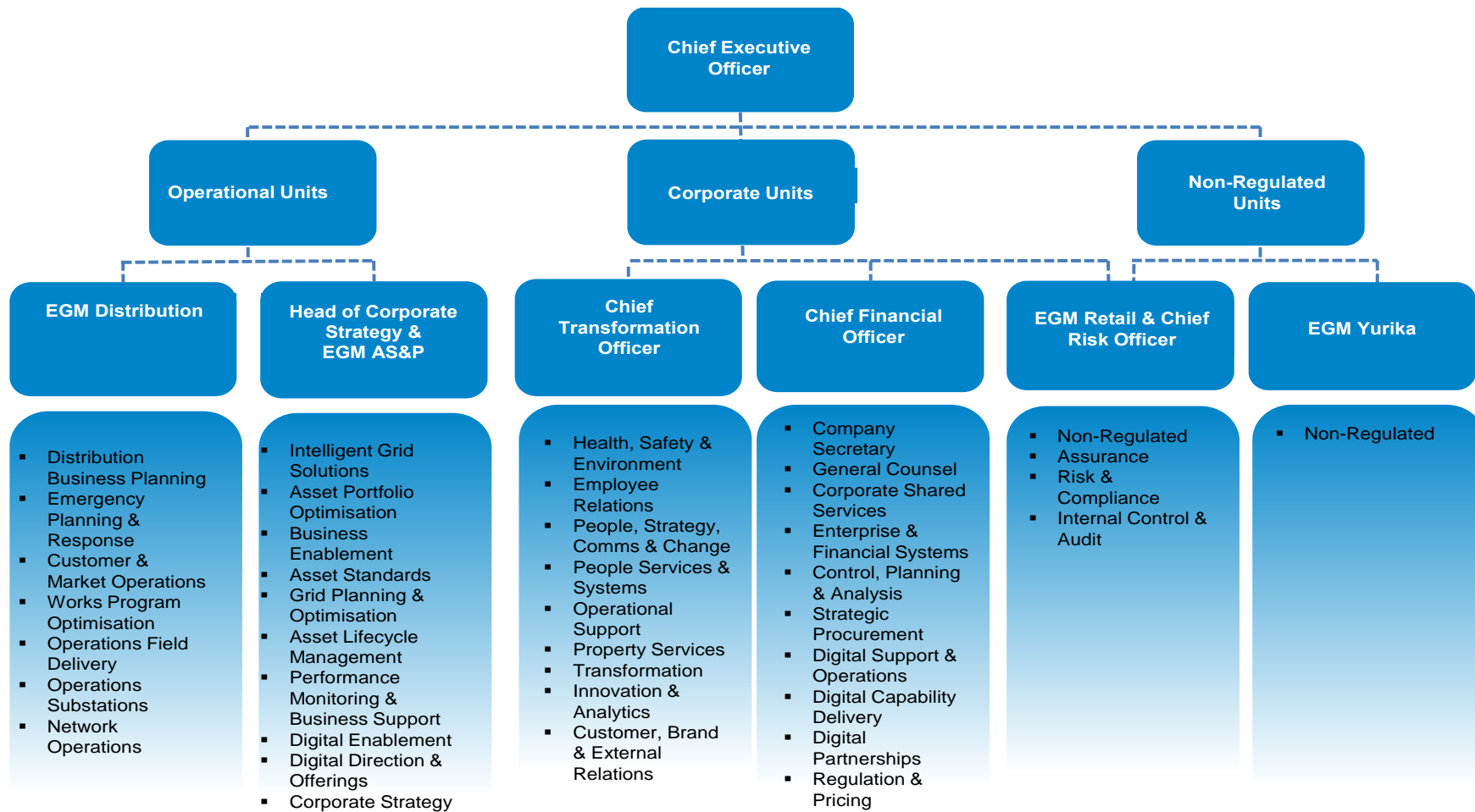
- provides a strong focus on continuous improvement and performance;
- aims to reduce costs and maximise operating synergies through streamlined decision making, common network management and IT activities;
- delivers economies of scale in procurement areas;
- seeks growth in new unregulated areas.

Operational units are split along the lines of asset management and field services, providing the efficient delivery of asset management, construction, maintenance and customer services to the group's two regulated distribution businesses and external customers.

Corporate units provide services to support the operational and non-regulated units and to meet the requirements of key stakeholders. The operational structure is described in more detail below. The business operation units are overseen and managed by the Chief Executive Officer (CEO) and Executive Leadership Team (ELT) comprising Executive General Managers from each respective business unit.

- Field Services - is the accountability of the Executive General Manager - Distribution and is focused on delivering customer needs by safely and efficiently designing, constructing, maintaining and operating the electricity network.
- Asset Management - is the accountability of the Head of Corporate Strategy & Executive General Manager Asset Safety and Performance and involves network strategic planning, network policies and standards development, work program governance, safety strategies, and network data management, digital enablement, digital direction & offerings, and corporate strategy.
- Customer, People and Culture – is the accountability of the Chief Transformation Officer and is focused on the provision of corporate human resource functions and payroll administration, occupational health and safety, environment and property services and operational support including fleet, supply, technical training and apprentices, innovation & analytics, customer, brand and external relations.
- Finance – is the accountability of the Chief Financial Officer and involves responsibility for the provision of financial accounting, management accounting, taxation, treasury, legal services, company secretariat and corporate shared services such as accounts payable and receivable, records management, insurance, digital support & operations, digital capability delivery, digital partnerships, and Regulation and Pricing.
- Risk and Audit – is the accountability of the EGM Retail and Chief Risk Officer and is focused on risk and compliance, internal control and audit functions.

Figure 2: Management Team and Functional Units



8 CATEGORIES OF DISTRIBUTION SERVICES

The classification of Energex's distribution services are outlined in the AER's "Final Decision - Energex determination 2016-16 to 2019-20 – Attachment 13 – Classification of Services" In accordance with the NER, the AER may classify distribution services as follows:

- Standard Control Services (SCS),
- Alternative Control Services (ACS),
- Negotiated Distribution Services, and
- Unclassified services.

Clause 3.2(a)(5) of the CAG requires the CAM to include a specification of the categories of distribution services that the DNSP provides to which costs are to be attributed and the types of persons to whom those services are provided.

Set out below are the categories of services provided by Energex. The services provided by Energex in each category are summarised in Table 1.

8.1 Standard control services (SCS)

Services associated with the access and supply of electricity to customers and includes the provision of network capability, maintenance and operation of the distribution system. These services are provided to all residential and business customers connected to the electricity network, the cost of which is recovered via Distribution Use of System (DUOS) tariffs.

8.2 Alternative control services (ACS)

Distribution services provided by Energex to specific customers where the customer is charged specifically for the service requested and includes the provision of metering and public lighting, connection services, and ancillary services. These services are provided to connected customers, third parties, and retailers, the cost of which is recovered by user pay fees or charges that apply to the specific customer requesting the service with the relevant charge being approved by the AER.

8.3 Unclassified services

Services which are capable of being provided on a contestable basis and includes the provision of Type 1-4 metering services. These services are not subject to economic regulation under the NER.

8.4 Other unregulated services

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

8.5 Negotiated services

Energex currently does not provide any services that are classified as negotiated services.

Table 1 – Network distribution services

Distribution Service Group	Service Description	AER Service Classification
Network services	Planning the network	SCS
	Designing the network	SCS
	Constructing the network	SCS
	Maintaining the network	SCS
	Operating the network for DNSP purposes	SCS
	Administrative support for the provision of network services	SCS
Pre-connection services	General connection enquiry services	SCS
	Connection application services	ACS
	Pre-connection consultation services	ACS
Connection services	Small customer connections	SCS
	Large customer connections	ACS
	Real estate development connection	ACS
	Removal of network constraint for embedded generator	ACS
	Temporary connections	ACS
Post connection services	Operate and maintain connection assets	SCS
Metering services	Connection management services	ACS
	Accreditation of alternative control service providers and approval of design works and materials	ACS
	Type 5 and 6 metering, maintenance, reading and data services (legacy meters)	ACS
	Type 7 metering services	SCS
	Auxiliary metering services	ACS
Street lighting services	Provision, construction and maintenance of street lighting	ACS
Ancillary network services	Services provided in relation to retailer of last resort event	ACS

Distribution Service Group	Service Description	AER Service Classification
	Other recoverable works	ACS
Unclassified distribution services	Type 1-4 metering	Unclassified
	Emergency recoverable works	Unclassified
	Watchman lights	Unclassified
	High load escorts	Unclassified

8.6 Types of persons to whom distribution services are provided

Energex provides distribution services to:

- Network customers: Energex provides a range of standard control and ACS to premises within its distribution area. ACS are requested through a retailer or in some circumstances can be requested directly by the customer.
- Third party customers: Energex provides alternative control services to third parties (e.g. local councils, real estate developers).
- Electricity retailers: Retailers purchase wholesale energy that is transported through Powerlink's transmission system, and Energex's distribution systems, to network connected customers. Retailers also request alternative control services (e.g. disconnection, special meter read) on behalf of customers.

9 COST ALLOCATION PRINCIPLES & POLICIES

9.1 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.

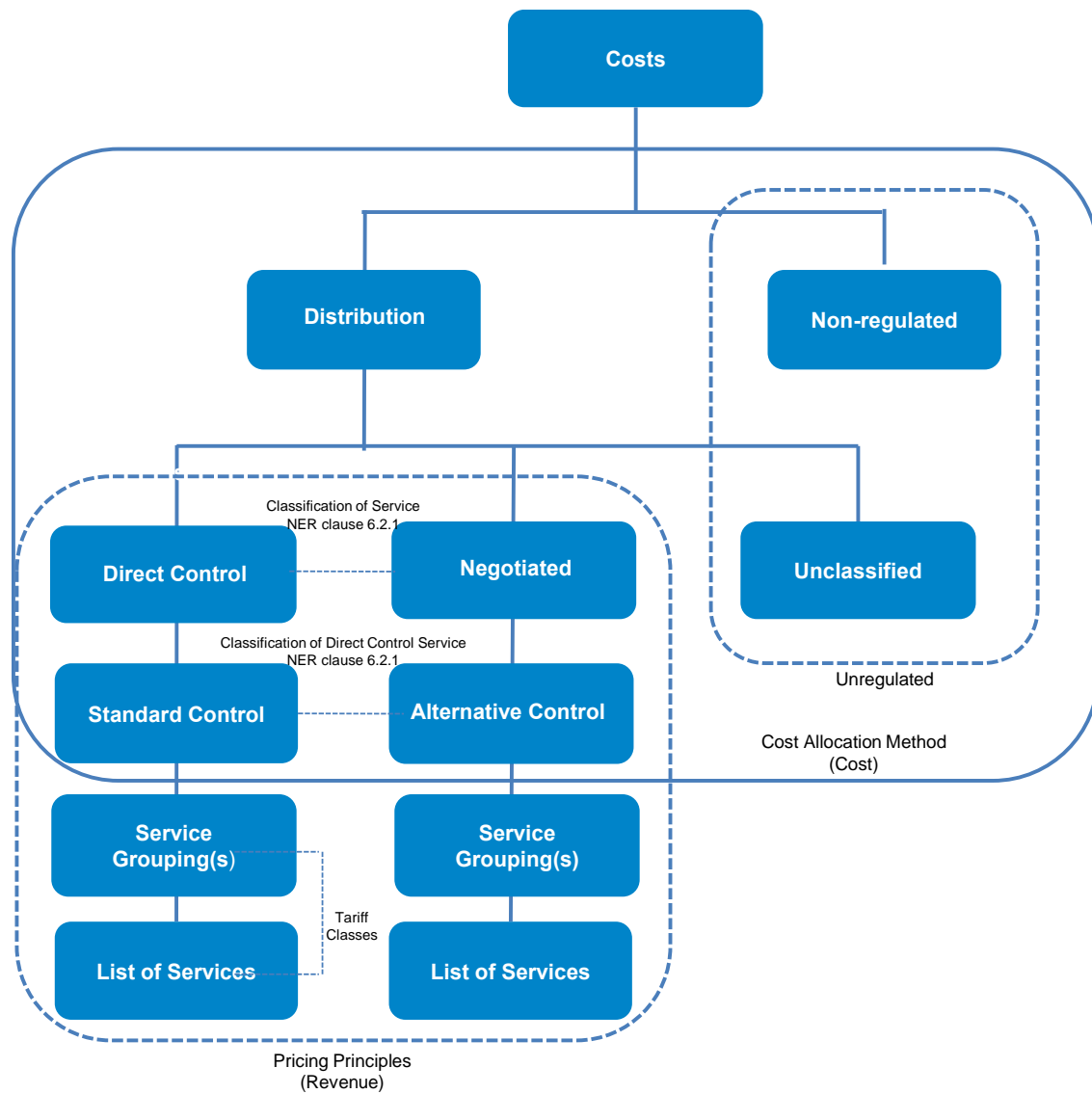
In accordance with the requirements of clause 2.2.2 of the Guidelines Energex confirms that the application of this CAM will facilitate the attribution of costs directly to, or allocate costs between categories of distribution services on the substance of the underlying transaction or event, rather than 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 3 represents a conceptual outline of the CAM as it applies to the various services outlined in Section 8. Further, it defines the point of interface between the CAM and Energex's pricing methodology. Figure 3 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 3: Conceptual model of interface to pricing model



9.2 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 9.4.
- **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 9.5.
- **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 9.7.
- **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 9.8.

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 B**.

9.3 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.

9.4 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 8 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 9.5 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 2 below provides further details on the allocation of direct costs.

Table 2 – 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.

9.5 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 10.

9.5.1 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:

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

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

9.5.2 Materials storage and logistics on-costs

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.

9.5.3 Fleet on-costs

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).

9.6 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 9.5.2 and 9.5.3 and are excluded from regulated overhead costs.
- Unregulated support costs, which are allocated to unregulated activities as detailed in sections 9.6.1 and 9.7 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 A**.

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 10.

9.6.1 Unregulated cost allocation

The unregulated cost allocation is based on the allocation process described in Section 9.7 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.

9.6.2 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 9.6 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, labor spend and material spend inclusive of on-costs) of the regulated distribution services.

The rate is calculated as follows:

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

9.7 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 9.2 direct costs (capex and opex) are attributed 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.

9.7.1 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.

9.8 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 periods 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.

10 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.

10.1 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 9.5. 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.

10.2 Regulated overhead pool

As stated above, this rate is based on budget data. The method for calculating the rate is discussed above in Section 9.6.2. 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.

10.3 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.

11 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 12.

12 WORK PAPERS

Applying, reconciling and auditing the CAM at an operational level within the business require 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.

13 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; and
- The basis of cost attribution or cost allocation being considered on the substance of the transaction over its legal form.

14 RECORD KEEPING

The Enterprise Resource Planning system (ERP) provides the capability to record and report financial information based on the CAM principles and policies for both statutory and regulatory purposes.

Outputs from this system include the standard suite of financial reports such as Trial Balance, General Ledger, Profit & Loss Statement, Balance Sheet and numerous other views of the posting of financial transactions (directly allocated and shared costs) which can be produced depending upon the nature of the enquiry. Transactions, once posted, cannot be deleted so that prior year data is therefore also maintained.

All records will be appropriately retained in accordance with regulatory and legislative requirements.

All information submitted to the AER through regulatory information notices is subject to external audit prior to submission.

15 MONITORING COMPLIANCE WITH THE CAM AND CAG

The Finance and Corporate Services Business Unit is responsible for monitoring compliance with the CAM for Energex. Operationally, the General Manager Financial Control will be responsible on a day to day basis for compliance.

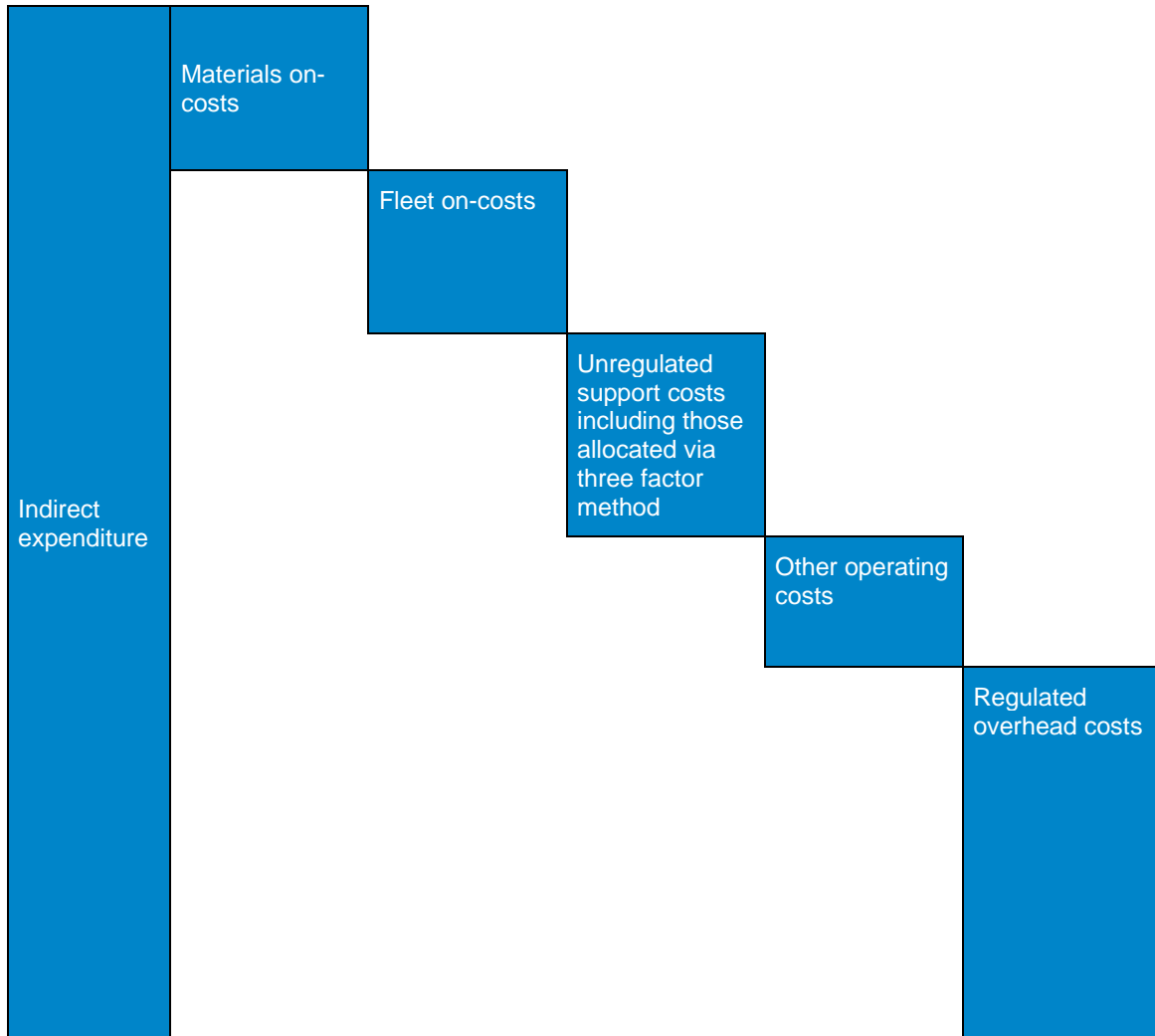
Energex's annual statutory financial statements and the ERP are reviewed by our external auditors.

Energex will undertake an independent audit of their 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. These include scheduled or ad hoc programs of specific areas identified by either management or shareholders.

APPENDICES

16 APPENDIX A: BREAKDOWN OF ENERGEX INDIRECT COSTS



17 APPENDIX B: COST ALLOCATION SUMMARY

Table AB.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)
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)

18 APPENDIX C: COMPLIANCE WITH CAG, RFG and NER

The following tables summarised the regulatory obligations and the demonstrated CAM compliance with the CAG, RFG and NER.

1. General obligations

Rules	CAG	Requirements	Addressed
6.15.4(f)(1)(ii)	1.5,3.1	An amended CAM must not take effect unless and until the DNSP notifies the AER of the agreement	This document
6.15.4(b)	1.5,3.1(b)	DNSP's proposed CAM must give effect to and be consistent with the CAG	This document
	5.4	DNSP must maintain current copy of approved CAM on its website	Version history and date of issue

2. Contents of Cost Allocation Method

CAG	RFG	Requirements	Addressed
3.2(a)(1)		Version number	Version history and date of issue
3.2(a)(2)		DNSP's commitment to history and date of issue	Version history and date of issue
3.2(a)(3)		Statement of nature, scope and purpose of document and way it is to be used	Section 5
3.2(a)(3)A		Accountabilities for implementation	Section 5
3.2(a)(3)B		Responsibilities for updating, maintaining and applying document and for internally monitoring and reporting its application	Section 5
3.2(a)(4)		Description of corporate and operational structure	Section 6, Section 7
3.2(a)(5)		Specification of service categories and types of persons to whom services provided	Section 8
3.2(a)(6)		Principles and policies for attributing costs to, and allocating costs between, categories of distribution services in accordance with clause 2.2 of CAG	Section 9
3.2(a)(7)	3.2.2(c)	Description of how will maintain records of attribution and allocation	Section 14

CAG	RFG	Requirements	Addressed
3.2(a)(8)	3.2.2(c)	Description of how will monitor compliance with CAM and CAG	Section 15
3.2(a)(9)		Commencement date	Section 4

3. Cost allocation principles and policies

Rules	CAG	RFG	Requirements	Addressed
6.15.2(1)	2.2.1(a)	3.2.2(a) and 3.2.2(b)	Include sufficiently detailed principles and policies for attributing costs to, and allocating costs between, categories of distribution services to enable: <ul style="list-style-type: none"> AER to replicate reported outcomes DNSP to demonstrate that it is meeting requirements 	Section 9 and Appendix B
	2.2.1(b)(1)		Include specified information on directly attributable costs to enable AER to replicate reported outcomes	Section 9.4
	2.2.1(b)(2)		Include specified information on shared costs to enable AER to replicate reported outcomes	Section 9
6.15.2(2)	2.2.2		Attribute costs directly to, or allocated costs between, categories of distribution services based on substance of underlying transaction or event not legal form	Section 9
6.15.2(3)(i)	2.2.3		Only directly attribute costs to categories of distribution services if they are directly attributable to the provision of the service	Section 9.4
6.15.2(3)(ii)	2.2.4		Allocate shared costs between categories of distribution services using an appropriate causal allocator, except to the extent that: <ul style="list-style-type: none"> Shared cost is immaterial Causal relationship cannot be established without undue cost or effort in which case may use non-causal allocator in specified circumstances	Section 9

Rules	CAG	RFG	Requirements	Addressed
6.15.2(4)			Clearly describe the cost allocation method, the reason for using it and the numeric quantity (if any) of the chosen allocator	Section 9
6.15.2(5)	2.2.5		Do not allocate the same cost more than once	Section 9
6.15.2(6)	2.2.6		Detailed principles, policies and approach used to attribute costs directly to, or allocated costs between, categories of distribution services must be consistent with the distribution ring fencing guidelines	Section 9
6.15.2(7)	2.2.7		Costs that have been attributed or allocated costs to distribution services must not be reattributed or reallocated to another service during the regulatory control period	Section 9