



Ergon Energy Regulatory Proposal (revised) 2015 to 2020

3 July 2015



Revision history

Version	Date	Summary of changes
1.0	31 October 2014	Initial Regulatory Proposal submitted to the AER
2.0	3 July 2015	Revised Regulatory Proposal submitted to the AER

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1. Introduction

Ergon Energy Corporation Limited's (Ergon Energy) Regulatory Proposal sets out our regulated distribution services and the revenue and prices associated with them for the regulatory control period commencing on 1 July 2015 and ending on 30 June 2020.¹

Our initial Regulatory Proposal was submitted to the Australian Energy Regulator (AER) on 31 October 2014.² The AER assessed our initial proposal and released its Preliminary Determination on 30 April 2015.

This document represents part of our submission to the AER on its Preliminary Determination.³ It is referred to as our revised Regulatory Proposal.⁴

Our proposal, and our overview of the proposal,⁵ complies with the requirements detailed in the National Electricity Rules (NER) and the National Electricity Law (NEL). This includes information we must provide in order for the AER to make the necessary decisions and determinations under the NER.

Our October Regulatory Proposal has been updated in parts to reflect the positions adopted by the AER in its Preliminary Determination. Where more up-to-date information is available, we have also incorporated this in our revised Regulatory Proposal.

We have not made revisions in circumstances where we have concerns with the AER's decision-making, or where we disagree with the substance of the issues raised by the AER. These concerns are detailed in our main submission and its individual submission documents.

In preparing our revised Regulatory Proposal, Ergon Energy has also taken into account stakeholder feedback.

1.1 Overview of our Regulatory Proposal

What we charge for the use of our network has fallen in 2015-16, in line with the AER's Preliminary Determination. For the remaining years of the regulatory control period 2015-20, Ergon Energy is targeting to keep what we charge for the use of our network at 2014-15 levels.

The following chart summarises the indicative movements in the aggregate network charges for the regulatory control period 2015-20, including annual increases in DUOS charges (excluding Solar Bonus Scheme feed-in tariff (FiT) costs) which represents the substance of our revised Regulatory Proposal and necessary adjustments to address the impacts of the AER's Preliminary Determination on our 2015-16 network charges.

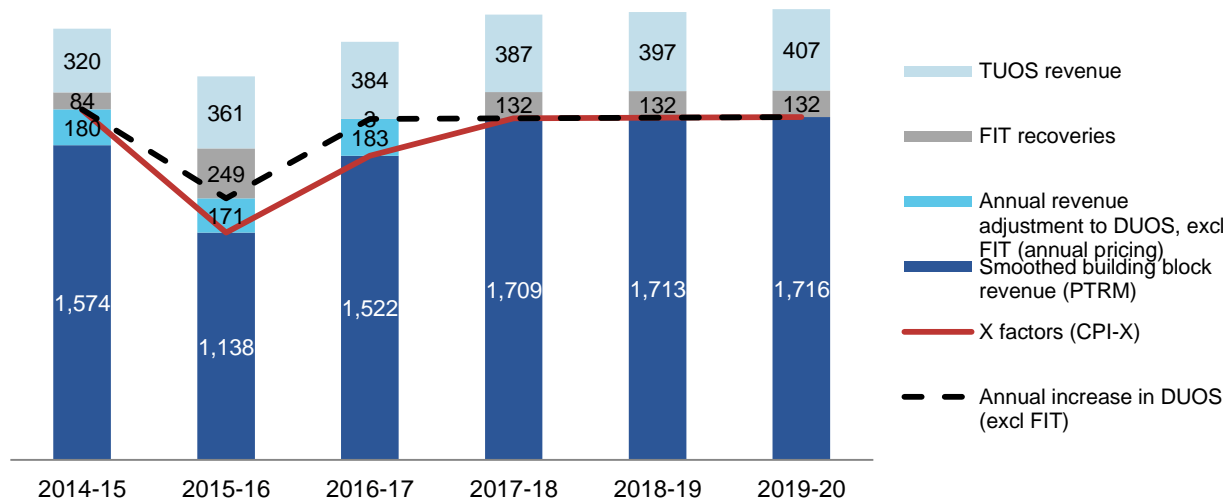
¹ This proposed term is consistent with the length of the regulatory control period 2010-15 and is the minimum duration for a regulatory control period permitted under clause 6.3.2(b) of the NER.

² <http://www.ergon.com.au/futureinvestment>.

³ NER, clause 11.60.4(b).

⁴ We use "Regulatory Proposal" and "revised Regulatory Proposal" interchangeably throughout this document.

⁵ 0A.00.01 – An Overview, Our Regulatory Proposal 2015-20 and 0A.00.01 – An Overview, Our Revised Plans 2015-20.



	2015-16	2016-17	2017-18	2018-19	2019-20
- - - Annual increase in DUOS (excl FIT)	(25.4%)	30.3%	0.2%	0.2%	0.2%
- - - X Factors (CPI - X)	36.6%	(30.5%)	(9.5%)	2.3%	2.3%

Figure 1: Movement in aggregate expected network charges, 2014-20 (\$m, nominal)⁶

We were optimistic in October 2014 that, with improving financial markets, the costs of financing our investments would fall. This has occurred and our required revenues are now lower than we forecast in our October Regulatory Proposal. We have updated our proposal to reflect these improved financing conditions. However, we have not made the equivalent changes to the rate of return parameters the AER determined in April 2015. The AER’s Preliminary Determination set these parameters too low.

Our revised capital expenditure forecasts are slightly lower, reflecting updated market expectation of cost inputs into the future. We have not adjusted these to the extent determined by the AER. The AER’s Preliminary Determination contained errors (which the AER has conceded) that will need to be adjusted in the Substitute Determination.

Depreciation schedules have been revised to account for the separation of asset classes into pre and post 2009 values. This resulted in a lower depreciation allowance to what we proposed in October Regulatory Proposal; reducing the amount of revenue we recover in the regulatory control period 2015-20.

Finally, we have changed our operating expenditure forecasts. However, we cannot accept the AER’s assessment process to be a reasonable one, having regard to our statutory requirements. We outline our main objections to the Preliminary Determination in our main submission, *Submission to the AER on its Preliminary Determination*, and supporting submissions.

⁶ Revenue from Type 5 and 6 metering installation, provision, maintenance, reading and data services was previously included in DUOS in 2014-15. Since these services will be Alternative Control Services in the regulatory control period 2015-20, revenue associated with these services has not been included in DUOS for 2015-20.

There have been substantial increases in the network component of customer electricity bills in the regulatory control period 2010-15. Through our engagement program, we have a clear understanding of the level of concern about rising electricity prices. We need to adjust the AER's determined total revenue allowance because it is too low. However, setting what we charge in 2016-17 lower than what we charged in 2014-15 and targeting charges for the remaining years of the regulatory control period 2015-20 to be at or below 2014-15 levels is in line with our commitment to delivering the best possible price.

Further, in formulating our plans we have also considered our commitments around delivering peace of mind, by way of a safe, dependable electricity service, and supporting greater customer choice and control in electricity supply solutions.

Our indicative analysis of the impact of distribution charges (excluding FiT adjustments) for a typical residential customer in the regulatory control period 2015-20 is shown in Table 1 below.

Table 1: Historic and proposed increases to our revenue requirements and associated residential price impact⁷

\$ nominal	Historic annual increases in 2011-15				Annual increases in 2015-20				
	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
% change	8%	9%	11%	10%	(26%)	29%	(6%)	1%	1%
\$ change	\$53	\$69	\$91	\$90	\$ (250)	\$212	\$ (57)	\$11	\$11
Estimated impact of DUOS increase on retail bill	4%	5%	6%	5%	(12%)	16%	(3%)	1%	1%

In addition to standard charges for use of the distribution network, Ergon Energy proposes:

- new charges for Type 5 and 6 meters in line with the AER's Preliminary Determination
- reductions to public lighting charges in 2015-16, as per the AER's Preliminary Determination, with charges adjusted in 2016-17 to reflect our actual costs. For the remaining years, charges will be maintained on a price path linked to the CPI
- other user specific charges, which are consistent with our approach in the regulatory control period 2010-15.

1.2 Documentation

1.2.1 Our submission on the AER's Preliminary Determination

Our high level response to the AER's Preliminary Determination is detailed in our document, *Submission to the AER on its Preliminary Determination*. This document highlights areas where Ergon Energy agrees or disagrees with the positions adopted by the AER in its Preliminary Determination and summarises our main concerns. It also responds, at a high level, to stakeholder

⁷ This table is based on the Queensland Competition Authority's (QCA) assumptions of a typical residential customer in Queensland consuming 4,091 kWh per annum (held constant). Indicative prices are based on assumptions of future revenue and volumes consistent with our Regulatory Proposal. Rates are indicative for the potential impact on a residential customer who is on a market retail contract and assumes the default network tariff applies. Customers on Notified Prices are on specific arrangements consistent with the Queensland Government's Uniform Tariff Policy. For further information on how regulated retail tariffs are determined go to <http://www.dews.qld.gov.au/energy-water-home/electricity/prices>.

feedback received to date on our October Regulatory Proposal and outlines our latest customer engagement activities.

We have provided more detailed information and reasoning behind our decision to agree or disagree with the AER's Preliminary Determination in supporting documents to our submission. These documents are categorised by topic (e.g. *Rate of Return (Cost of Equity) – Response*). Revisions to our initial proposal are clearly identified in these documents. A number of other documents are also provided which support the arguments presented in the detailed submissions by topic.

Finally, we have submitted this revised Regulatory Proposal. It takes the form of the Regulatory Proposal we submitted in October 2014, but it has been updated as necessary to reflect our response to the AER's Preliminary Determination and any other updated information. Documents that accompanied our October Regulatory Proposal have also been resubmitted, either in their current form or updated to reflect new numbers and/or approaches.

A graphical depiction of the suite of information accompanying our submission to the AER is shown in Figure 2.

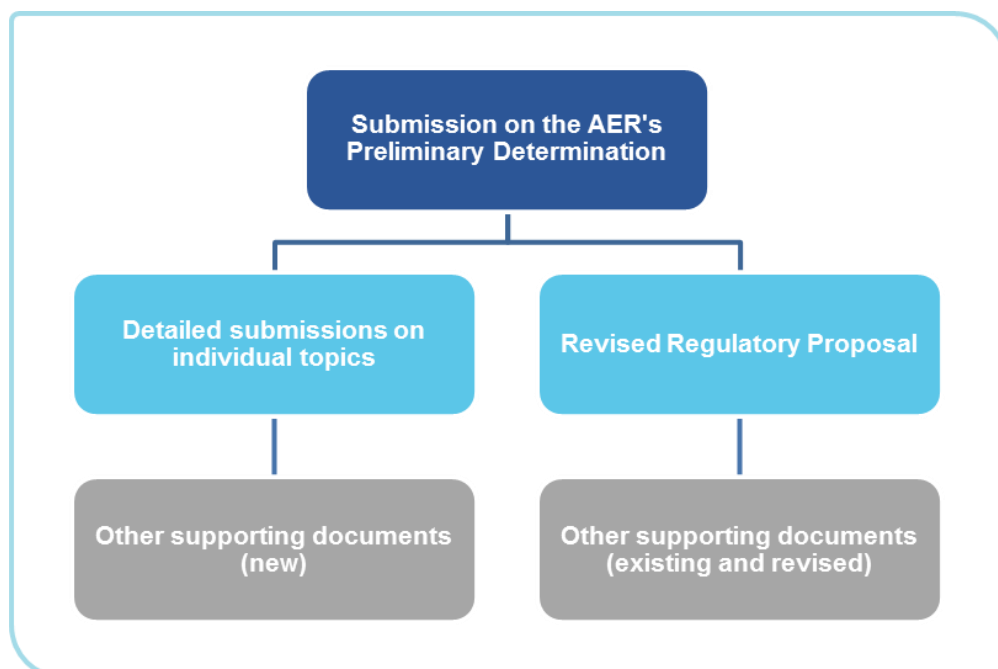


Figure 2: Overall structure of our submission to the AER

1.2.2 Regulatory Proposal documentation

The information requirements for our Regulatory Proposal are extensive.⁸ Our Regulatory Proposal therefore includes this main proposal document (including appendices), our overview and a series of supporting documents, attachments, models and reference material which provide information addressing specific regulatory issues and requirements, business as usual policies, procedures and practices, and financial and regulatory models. Each of these documents should be considered by the AER in making its Distribution Determination.

⁸ Clause 6.8.2(c) of the NER dictates what a regulatory proposal must include. Other information is also provided to comply with the NER and to assist the AER perform its functions under the NEL.

Accompanying our Regulatory Proposal are the following documents:

- *An Overview, Our Revised Plans 2015-20*,⁹ summarising key matters of importance to electricity customers¹⁰
- further supporting information to assist our customers understand how they have informed our plans, our response to the challenge of providing services to our customers in a changing energy market, and how we have arrived at our proposed prices
- information required by the Regulatory Information Notice (RIN) under clause 6.8.2(d) of the NER.¹¹ The RIN is used by the AER to collect information it considers necessary to assess our Regulatory Proposal. We have addressed the requirements of the RIN in this Regulatory Proposal and our supporting documents.¹²

A graphical depiction of the suite of information prepared with our Regulatory Proposal is provided in Figure 3.

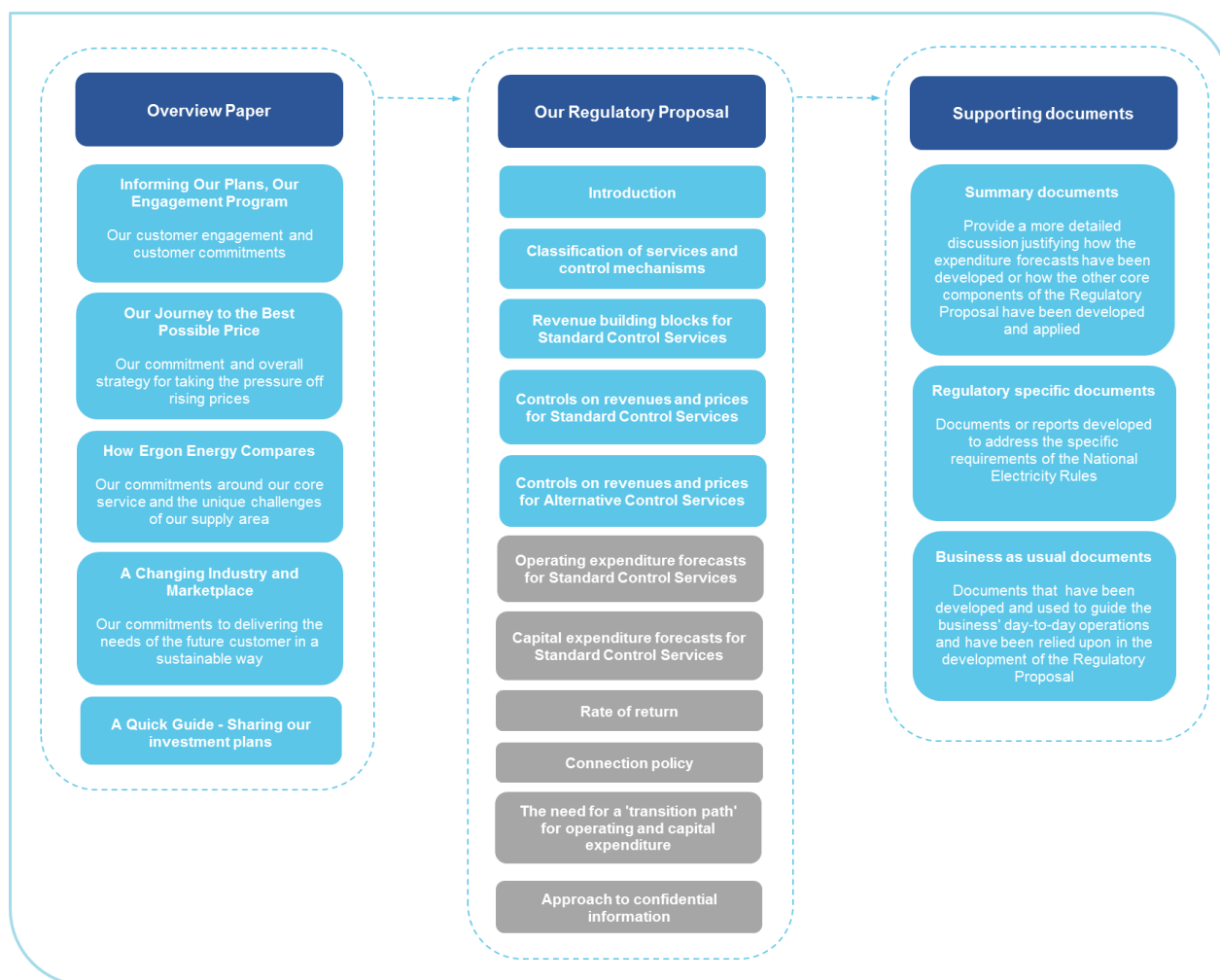


Figure 3: Overall structure of our Regulatory Proposal package

⁹ 0A.00.01 – *An Overview, Our Regulatory Proposal 2015-20* and 0A.00.01 – *An Overview, Our Revised Plans 2015-20*.

¹⁰ This includes the matters required under clause 6.8.2(c1) of the NER.

¹¹ Ergon Energy assumes the AER's instrument covers the information the AER requires under clause 6.8.2(c2) of the NER, consistent with the AER's Framework and Approach Paper.

¹² Except for material changes, our response to the RIN has not been updated since our October Regulatory Proposal. For the avoidance of doubt, the RIN response was submitted following a formal request from the AER in August 2014. It is not required for our revised Regulatory Proposal.

1.3 Ergon Energy as a business

Ergon Energy is a Queensland Government-owned corporation whose principal activity is the operation of the electricity distribution system in regional Queensland. Ergon Energy holds a Distribution Authority, administered by the Director-General of the Queensland Department of Energy and Water Supply, to perform this function.

We supply electricity across a service area of more than one million square kilometres – 97% of the state of Queensland. Around 70% of the network's powerlines are considered rural, with a very low customer density and largely radial profile. We have a team of 4,415 employees who live by our values to safely deliver more than 15,000GWh of electricity annually to around 725,000 customers.

In addition to our grid-connected distribution system, the AER is responsible for the economic regulation of the Mount Isa–Cloncurry network.¹³ Accordingly, Ergon Energy has included the Mount Isa–Cloncurry network in this Regulatory Proposal.¹⁴ This is consistent with the approach adopted in the AER's Distribution Determination for the regulatory control period 2010-15.

Ergon Energy has included a supporting document, *How Ergon Energy Compares*,¹⁵ which provides more information on our distribution business, customers, network and operating environment.

In addition to our core distribution business, Ergon Energy owns and operates:

- Ergon Energy Queensland Pty Ltd (EEQ), which provides electricity retail services to non-market customers in our distribution area. EEQ owns and operates the Barcaldine Power Station
- Ergon Energy Telecommunications Pty Ltd (EET), which services our communication needs and, as a licensed telecommunications carrier, offers the Queensland marketplace wholesale high-speed data services.

Ergon Energy is also a shareholder of SPARQ Solutions Pty Ltd (SPARQ), a joint venture with Energex Limited (our south-east Queensland counterpart), which provides information and communications technology (ICT) solutions and services to both organisations.

EET and EEQ's services are not regulated by the AER and are not covered in this Regulatory Proposal. However, some of SPARQ's ICT services are related to the provision of distribution services by Ergon Energy and are reflected accordingly in our Regulatory Proposal.

1.4 Other relevant matters

1.4.1 Framework and Approach

A Framework and Approach Paper is a document published before a Regulatory Proposal is submitted which sets out the AER's decisions and proposed approaches to a number of matters relevant to the Distribution Determination, such as the classification of distribution services, the forms of control to be applied and the application of incentive schemes.

¹³ Section 10 of the *Electricity National Scheme (Qld) 1997* treats the Mount Isa-Cloncurry supply network (which is not connected to the national grid) as a distribution system as if it were part of the national grid.

¹⁴ Ergon Energy requests that the AER have regard for clause 6.8.2(e) of the NER and make a determination that Ergon Energy shall make one Regulatory Proposal that encompasses both the grid-connected network and the Mount Isa-Cloncurry network.

¹⁵ Refer to *0A.01.01 – How Ergon Energy Compares*.

The AER issued the Framework and Approach Paper for Ergon Energy on 30 April 2014.¹⁶ Ergon Energy took the outcomes of the AER's Framework and Approach Paper into account in preparing the October Regulatory Proposal. In its Preliminary Determination, the AER departed from the Framework and Approach Paper in some areas. To the extent we have agreed with those departures, we have updated our revised Regulatory Proposal accordingly.

1.4.2 Expenditure Forecast Methodology

On 29 November 2013, Ergon Energy notified the AER of the methodologies we proposed to use to forecast our capital and operating expenditure for the regulatory control period 2015-20. Our Expenditure Forecast Methodology¹⁷ was developed in accordance with the NER and the AER's Expenditure Forecast Assessment Guideline. A copy of our Expenditure Forecast Methodology is available on our website.¹⁸

Our forecasts are broadly consistent with the forecasting method established in the Expenditure Forecast Methodology. We explain how Ergon Energy's Expenditure Forecast Methodology is applied to our operating and capital expenditure forecasts (including any departures from our published methodology) in Appendix A and Appendix B, respectively, and our summary documents.

1.4.3 Sunset of transitional arrangements for regulatory control period 2010-15

Clause 11.16 of the NER sets out the transitional arrangements for the first Distribution Determination made by the AER for the Queensland Distribution Network Service Providers (DNSPs). These transitional arrangements applied for the regulatory control period 2010-15 and cease to have effect from 1 July 2015. In addition, changes to the NER during the regulatory control period 2010-15 resulted in a number of transitional arrangements which will also cease to have effect from 1 July 2015.

The transitional arrangements related to the following matters:

- the treatment of assets included in the Regulatory Asset Base (RAB)¹⁹
- Capital Contributions Policy and treatment of capital contributions in the RAB²⁰
- Efficiency Benefit Sharing Scheme (EBSS)²¹
- Service Target Performance Incentive Scheme (STPIS)²²
- jurisdictional schemes²³
- the recovery of charges for using the non-regulated 220 kV network which supplies the Cloncurry township²⁴

¹⁶ Available at <http://www.aer.gov.au/node/20186>.

¹⁷ As required by clause 6.8.1A of the NER.

¹⁸ Refer to <https://www.ergon.com.au/network/network-management/future-investment/future-direction>.

¹⁹ NER, clause 11.16.3.

²⁰ NER, clauses 11.16.10 and 11.46.6.

²¹ NER, clause 11.16.4.

²² NER, clause 11.16.5.

²³ NER, clause 11.35.

²⁴ NER, clause 11.39.6.

- the recovery of entry and exit charges relating to non-prescribed connection points between Powerlink’s transmission network and our distribution network.²⁵

Further information on the cessation of these transitional arrangements and how they impact the Regulatory Proposal is contained in our supporting document *01.01.02 – (Revised) The Effect of Transitional Arrangements*.

1.4.4 Transitional arrangements for regulatory control period commencing 1 July 2015

Clause 11.60 of the NER sets out the transitional provisions that apply to Ergon Energy for the regulatory control period 2015-20. The transitional provisions effectively provide that a final Distribution Determination (the Preliminary Determination) will be made by the AER by 30 April 2015, with a revocation and substitution of the Preliminary Determination (the Substitute Determination) by 31 October 2015.²⁶

Because the Substitute Determination is made after the commencement of the regulatory control period 2015-20, adjustments may be necessary to account for changes between the Preliminary and Substitute Determination.²⁷

1.4.5 Legislative and regulatory obligations

Ergon Energy must comply with numerous legislative and regulatory obligations, and Queensland Government policy requirements, in the regulatory control period 2015-20. Some of these obligations directly impact our expenditure forecasts. Our supporting document *01.01.01 – (Revised) Legislative and Regulatory Obligations and Policy Requirements* provides further information on the obligations applicable to Ergon Energy.

We have also provided more detail around specific obligations relevant to:

- capital expenditure forecasts in Appendix B and in relevant supporting documentation for each capital expenditure category
- operating expenditure forecasts in Appendix A and in relevant supporting documentation
- public lighting and metering services in Chapter 5 and in relevant supporting documentation.

1.4.6 Compliance with NER requirements

The supporting evidence in our Regulatory Proposal package which demonstrates compliance with our relevant compliance obligations under Chapter 6 of the NER is detailed in our supporting document *01.02.01 – NER Compliance Matrix*. We have done this in order to assist the AER undertake its preliminary examination of the Regulatory Proposal.²⁸

1.4.7 Negotiating framework

Neither the AER nor Ergon Energy have proposed that any services be classified as negotiated distribution services in the regulatory control period 2015-20. In its Framework and Approach

²⁵ NER, clause 11.39.6.

²⁶ NER, clause 11.60.4(c).

²⁷ Our supporting document *04.01.00 – (Revised) Compliance with Control Mechanisms* provides some detail on how this will apply.

²⁸ NER, clause 6.9.1.

Paper, the AER decided to maintain its current position that a distributor need not submit a negotiating framework if it does not provide negotiated services.²⁹

Since that time, the AER has revised its position and has informally requested Ergon Energy to submit a negotiating framework. We understand the AER is requesting us to provide a negotiating framework for its own compliance purposes. Our negotiating framework can be found at supporting document *01.01.03 – Ergon Energy’s Negotiating Framework*.

1.4.8 Confidential information

The information contained in this main proposal document is public information. However, some of the information in documents supporting our Regulatory Proposal is information that Ergon Energy considers to be confidential information.

Our specific confidentiality request and claims, which are made in accordance with the AER’s Confidentiality Guideline, are summarised in Appendix F.

1.5 Additional matters since submission of our initial proposal

1.5.1 Stakeholder consultation

There has been considerable stakeholder consultation since the submission of our initial Regulatory Proposal on 31 October 2014. Ergon Energy has considered this feedback in developing our revised Regulatory Proposal.

Issues Paper and public forum

In December 2014, the AER released its Issues Paper on Ergon Energy’s October Regulatory Proposal.³⁰ The Issues Paper aimed to assist stakeholders by setting out the key preliminary issues on which they should engage and comment. It focused on our proposed capital and operating expenditure forecasts, and the rate of return. The AER received 31 stakeholder submissions, including a submission from Ergon Energy.³¹

The AER also held a public forum on 9 December 2014, which provided stakeholders and the Consumer Challenge Panel (CCP) with an opportunity to comment on the October Regulatory Proposal.

Metering Consultation Paper

In its draft decisions for New South Wales (NSW) and the Australian Capital Territory (ACT), the AER rejected the proposed metering exit fees on the basis that a large metering exit fee would create a barrier to competition. Instead, the AER proposed to recover the residual capital costs of a meter when a customer transferred to an alternative provider as a Standard Control Service.

A number of concerns were raised in response to this position. Consequently, in March 2015, the AER released a Consultation Paper on an alternative mechanism for the recovery of these costs in NSW, the ACT, Queensland and South Australia.³² The AER proposed to recover these costs

²⁹ AER (2014a), *Final Framework and approach for Energex and Ergon Energy, Regulatory control period commencing 1 July 2015*, April 2014, p154.

³⁰ AER (2014), *Issues Paper, Queensland electricity distribution regulatory proposals 2015-16 to 2019-20*, December 2014.

³¹ See www.aer.gov.au/node/20186.

³² AER (2015), *Alternative approach to the recovery of the residual metering capital costs through an alternative control services annual charge*, March 2015.

from both current and churned metering customers, as an annual Alternative Control Service charge.

Nineteen submissions were lodged on the Consultation Paper, including a submission from Ergon Energy.³³

Consumer Challenge Panel

The CCP sub-panel was appointed by the AER to provide advice on the effectiveness of our customer engagement and to provide input on issues of importance to customers. In addition to highlighting their initial observations at the public forum in December 2014,³⁴ the CCP sub-panel lodged two submissions in response to our October Regulatory Proposal.³⁵

Ergon Energy also met with Hugh Grant, a CCP sub-panel member, in April 2015 to discuss our proposal in relation to the STPIS, demand management, capital expenditure, operating expenditure and the rate of return.

Customer engagement

Since submitting our Regulatory Proposal in October 2014, Ergon Energy has continued to engage with customers and stakeholders, explaining our positions and providing additional information and reasoning where necessary. We have also engaged with customers on the outcomes of the AER's Preliminary Determination and Ergon Energy's likely response. Our submission on the AER's Preliminary Determination provides detail of our engagement arrangements.

1.5.2 AER assessment process

In undertaking its assessment of our October Regulatory Proposal, the AER and its consultants met with Ergon Energy representatives and formally asked Ergon Energy almost 70 questions (with numerous sub-parts) on various aspects of our proposal. We have amended our October Regulatory Proposal to reflect the outcomes of this process, where required.

1.5.3 AER Preliminary Determination for Queensland

The AER released its Preliminary Determination for Ergon Energy on 30 April 2015.³⁶ The Preliminary Determination sets out the revenue Ergon Energy is allowed to recover from customers in 2015-16 for the provision of regulated distribution services, as well as the prices that can be charged for some of these services.³⁷

Ergon Energy has carefully reviewed the AER's Preliminary Determination. Where we agree with the positions adopted by the AER, we have made changes in this revised Regulatory Proposal.

³³ http://www.aer.gov.au/sites/default/files/Ergon%20Energy%20%282%29%20-%20Submission%20in%20response%20to%20AER%20consultation%20paper%20-%20Recovery%20of%20residual%20metering%20costs%20%20-%2027%20March%202015_4.pdf.

³⁴ See www.aer.gov.au/node/20186.

³⁵ Bruce Mountain (2015), *CCP Sub-Panel submission on Energex, Ergon and SAPN revenues controls*; and Hugh Grant (2015), *Consumer Challenge Panel (CCP2 Panel) Submission on Energex and Ergon Energy Capex and Opex Proposals*, 30 January 2015.

³⁶ Available at <http://www.aer.gov.au/node/20186>.

³⁷ The revenues and prices to apply in 2016-17 to 2019-20 will be set out in the AER's Substitute Determination. These revenues may include any corrections for the 2015-16 year.

1.5.4 AER decisions in other jurisdictions

A number of regulatory determination consultation processes are occurring in other jurisdictions at the same time as our own process. In some circumstances, the issues raised in these processes are similar to our own. To assist in those processes, we have provided additional evidence by way of submissions that are also relevant to our determination process.

Ergon Energy made submissions to the AER on various determinations, including:

- the NSW and ACT electricity distribution networks
- the Jemena gas network in NSW.

On the AER's decision on rate of return, we have jointly engaged expert advice since the concerns with the AER's decision on rate of return are common across many network businesses. The expert advice is attached to our submission.

1.6 Supporting documentation

The following documents referenced in this chapter accompany our Regulatory Proposal:

Name	Ref	File name
An Overview, Our Revised Plans 2015-20	0A.00.01	An Overview Our Revised Plans
Regulatory Information Notice	N/A	Our response to the AER's RIN is contained in a number of files attached to this proposal. Information provided in our RIN is correct as at the time of our October Regulatory Proposal, unless otherwise stated
How Ergon Energy Compares	0A.01.01	How Ergon Energy Compares
(Revised) Legislative and Regulatory Obligations and Policy Requirements	01.01.01	(Revised) Legislative and Regulatory obligations
(Revised) The Effect of Transitional Arrangements	01.01.02	(Revised) Effect of Transitional Arrangements
Ergon Energy Negotiating Framework	01.01.03	Negotiating Framework
NER Compliance Matrix	01.02.01	Compliance checklist
(Revised) Compliance with Control Mechanisms	04.01.00	(Revised) Compliance with control mechanisms
Submission to the AER on its Preliminary Determination	N/A	Submission to the AER on its Preliminary Determination