01.01.02

The Effect of Transitional Arrangements

Revision history

Version	Date	Summary of changes
1.0	31 October 2014	As submitted to the AER as part of the initial Regulatory Proposal
2.0	3 July 2015	Updated to reflect the AER's Preliminary Determination in relation to the treatment of costs associated with Chumvale and non-prescribed Powerlink connection points. Minor drafting amendments have also been made.

Contents

1. Introduction

1.1 Overview

Clause 11.16 of the National Electricity Rules (NER) sets out the transitional arrangements for the first Distribution Determination made by the Australian Energy Regulator (AER) for the Queensland Distribution Network Service Providers (DNSPs). These transitional arrangements applied during the regulatory control period 2010-15 and will cease to have effect in the regulatory control period 2015-20. 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.

1.2 Rule requirements

The AER issued Ergon Energy with a Regulatory Information Notice (RIN) under Division 4 of Part 3 of the National Electricity (South Australia) Law (Qld) that requires Ergon Energy to provide the information specified in the RIN.

For transitional arrangements, the RIN requires Ergon Energy to:

34.1 Provide information on transitional issues (expressly identified in the Rules or otherwise) which Ergon Energy expects will have a material impact on it and should be considered by the AER in making its distribution determination. For each issue, set out the following information:

(a) the transitional issue;

(b) what has caused the transitional issue;

(c) how the transitional issue impacts on Ergon Energy; and

(d) how Ergon Energy considers the transitional issue could be addressed.

This attachment addresses the above requirements for each of the transitional arrangements identified by Ergon Energy.

1.3 Transitional arrangements

The transitional arrangements set out in clause 11.16 of the NER related to the following matters:

- the treatment of certain assets included in the Regulatory Asset Base (RAB)
- capital contributions policy
- Efficiency Benefit Sharing Scheme (EBSS)
- Service Target Performance Incentive Scheme (STPIS)
- jurisdictional schemes
- the recovery of charges for using the non-regulated 220 kV network which supplies the Cloncurry township (Chumvale)
- the recovery of entry and exit charges relating to non-prescribed connection points between Powerlink's transmission network and our distribution network (Powerlink).

In addition, there are transitional arrangements set out in clause 11.60 of the NER relating to the timing and application of the AER's distribution determination for 2015-20, and arrangements in clause 11.46 of the NER relating to interim connection charging rules.

2. Effect of transitional arrangements

The following sections summarise the effects of the cessation of the transitional arrangements on Ergon Energy's Regulatory Proposal.

2.1 Shared assets in the RAB

Clause 11.16.3 of the NER required the AER to accept the approach proposed by Ergon Energy in the regulatory control period 2010-15 regarding the treatment of certain assets in the RAB, provided the approach was consistent with the 2005 determination. As a result, some assets were included in the RAB that were used to provide services other than just Standard Control Services. This was consistent with legacy regulatory arrangements.

Under clause 6.5.1(a) of the NER, assets must only be included in the RAB to the extent that they are used to provide Standard Control Services. In its final Framework and Approach paper, the AER stated that we should provide an updated Cost Allocation Method (CAM) and establish our RAB for the regulatory control period 2015-20 with asset costs allocated to service types, with verification by an audit process.[1]

For the regulatory control period 2015-20, the cost of new assets will be allocated between Standard Control Services and other services in accordance with our revised CAM. The new CAM was approved by the AER and will take effect from 1 July 2015.

We propose to retain in the opening RAB for the regulatory control period 2015-20 those assets that are used to provide services other than Standard Control Services, consistent with the arrangements in 2010-15. To ensure that our customers do not pay for these assets twice and are no worse off than under the 2010-15 Distribution Determination, we propose to apply an offsetting revenue adjustment. This adjustment is equivalent to the sum of the depreciation and return on assets, for the component of the shared assets that are used for purposes other than Standard Control Services.

Further information on the calculation of the revenue adjustment to account for those assets in the RAB that are used to provide services other than Standard Control Services is provided in chapter 3 of our Regulatory Proposal or in our supporting document *03.01.02 – (Revised) Other Revenue Adjustments*.

2.2 Capital contributions policy

Transitional clause 11.16.10 of the NER required Ergon Energy to comply with a capital contributions policy in the regulatory control period 2010-15. This policy must be based on the Network Pricing Principles Statements approved by the Queensland Competition Authority immediately in force prior to 1 July 2009. Clause 11.16.10 also provides mechanisms for the AER or us to modify this policy if necessary.

This transitional clause will no longer have any effect from 1 July 2015. Rather, in the regulatory control period 2015-20, Ergon Energy will be required to prepare a connection policy in accordance with clause 6.7A.1 of the NER.[2] This connection policy incorporates our approach to capital contributions, consistent with the AER's Connection Charge Guidelines.[3]

[1] AER (2014), *Final Framework and approach for Energex and Ergon Energy, Regulatory control period commencing 1 July 2015,* April 2014, p158.

[2] This is the result of the introduction of the National Energy Customer Framework in Queensland from 1 July 2015.

[3] AER (2012), *Connection charge guidelines for electricity retail customers,* June 2012.

Our proposed connection policy is included in our supporting document *09.01.01 – (Revised) Ergon Energy Connection Policy*.

2.3 Efficiency Benefit Sharing Scheme

In its final Framework and Approach paper, the AER decided to apply the EBSS to Ergon Energy in the regulatory control period 2015-20. However, the AER departed from this position in its Preliminary Determination and decided it would not apply. Ergon Energy does not accept this departure. It is therefore necessary to identify the impact of the cessation of transitional arrangements on our Regulatory Proposal.

Transitional clause 11.16.4 of the NER stipulated that an EBSS for Ergon Energy in the regulatory control period 2010-15 was not to cover efficiency gains and losses related to capital expenditure. It further required the AER to have regard to the obligations on us in the regulatory control period 2010-15 to implement the recommendations of the Queensland Government's Electricity Distribution and Service Delivery for the 21st Century review (EDSD Review).

In the regulatory control period 2015-20, the EBSS will continue to exclude efficiency gains and losses related to capital expenditure. This is because new clause 6.5.8 of the NER explicitly limits the application of the EBSS to operating expenditure only. This is consistent with the AER's final Framework and Approach paper which states the EBSS will only apply to operating expenditure efficiency gains and losses. [4]

However, we note that the AER will apply a new Capital Expenditure Sharing Scheme (CESS). [5] This means that we will be subject to an incentive scheme on capital expenditure in the regulatory control period 2015-20, but not by virtue of the transitional arrangements ceasing to apply.

There will be minimal impact from the AER not needing to take into consideration the recommendation of the EDSD Review for the EBSS, as these recommendations do not affect our operating expenditure forecasts for the regulatory control period 2015-20.

We further consider the proposed application of incentive schemes, including the EBSS and the CESS, in chapter 3 of our Regulatory Proposal and, or in our supporting document *03.01.03 – (Revised) Application of Incentive Schemes*.

2.4 Service Target Performance Incentive Scheme

Clause 6.6.2 of the NER sets out the factors the AER must take into consideration in the development of a STPIS. In the regulatory control period 2010-15, the AER was required by transitional clause 11.16.5 of the NER to take into account a number of extra factors when making its decision on the application of a STPIS to Ergon Energy. These additional factors were:

- the obligations on us in the regulatory control period 2010-15 to implement the recommendations of the Queensland Government's Electricity Distribution and Service Delivery for the 21st Century review
- the impact of severe weather events on service performance
- whether the scheme should be applied as a paper trial or whether a lower powered incentive is appropriate.

[4] AER (2014), *Final Framework and approach for Energex and Ergon Energy, Regulatory control period commencing 1 July 2015,* April 2014, p75.

[5] Ibid p82.

With the passing of this transitional clause, the AER is no longer required to take into account the extra factors as detailed above in its application of an STPIS. In the regulatory control period 2015-20, the AER will make and implement a STPIS in accordance with clause 6.6.2 of the NER. This means that, in the regulatory control period 2015-20, Ergon Energy may be subject to potential penalties resulting from under performance due to severe weather events.

Further detail on our proposed approach to the application of incentive schemes, including the STPIS, is provided in chapter 3 of our Regulatory Proposal, or in our supporting document *03.01.03 – (Revised) Application of Incentive Schemes*.

2.5 Jurisdictional schemes

Although not a transitional requirement specified in the NER, we note that there will be a change in the regulatory control period 2015-20 in how the costs from the Queensland Solar Bonus Scheme (SBS) will be treated.

In the regulatory control period 2010-15, differences between the feed-in tariff (FiT) amounts that we forecast and the actual amounts that we paid have been recovered by way of a nominated pass through event. This method of recovery was approved by the AER in its 2010-15 Distribution Determination.[6]

The method of recovery of jurisdictional scheme amounts affects the way we price our services and the planning of our cash flows.

In the regulatory control period 2015-20, the SBS will be treated as a jurisdictional scheme under clause 6.18.7A of the NER and we will recover the FiT payments we make through our annual pricing proposal process. Further, to avoid recovering both FiT pass through amounts and SBS jurisdictional scheme amounts in the same years, we propose to recover the jurisdictional scheme amounts from customers under a two year lag approach.

Further information on how we will treat the SBS and other jurisdictional schemes is set out in chapter 4 of our Regulatory Proposal and our supporting document *04.01.02 – (Revised) Jurisdictional Schemes*.

2.6 Chumvale and non-regulated connection points

Ergon Energy owns an unregulated network represented by a 105km 220kV line from the Mica Creek “C” Switchyard at Mount Isa up to and including an unregulated 220/66kV substation at Chumvale. This network supplies a number of very large directly connected customers through unregulated arrangements.

Some of these Chumvale unregulated assets also provide network support to the Cloncurry township which forms part of the Mount Isa-Cloncurry network that is subject to economic regulation under the NER.

Under clause 11.39.6 of the NER, charges for the use of Chumvale are treated as designated pricing proposal charges for the regulatory control period 2010-15. In other words, transitional arrangements allow Ergon Energy to charge distribution customers for the use of the Chumvale unregulated network. The costs are included as a Transmission Use of System charge in our network tariffs. This means Chumvale takes on the same characteristics of the charges we pay to Powerlink and pass onto customers in other parts of the network.

[6] AER (2010), *Final Decision: Queensland Distribution Determination, May 2010*, pp311-312.

Clause 11.39.6 of the NER also allows Powerlink charges for entry and exit services at four[7] non-prescribed connection points between Powerlink's transmission network and our distribution network to be treated as designated pricing proposal charges for the regulatory control period 2010-15.

These transitional arrangements will cease to apply from 1 July 2015. However, in its Preliminary Determination, the AER decided to continue to treat these costs as designated pricing proposal charges. Ergon Energy has applied the AER's interpretation in our Regulatory Proposal.

We provide further detail in our supporting document *04.01.01 – (Revised) Designated Pricing Proposal Charges*.

2.7 Timing of distribution determination

Clause 11.60 of the NER sets out the special transitional provisions regarding the making of a distribution determination for Ergon Energy (and Energex and SA Power Networks) 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. They remove the necessity of the AER to make a draft distribution determination.

Although the Substitute Determination will not be made until after the commencement of the regulatory control period 2015-20, it will be applied as from 1 July 2015. As such a 'true-up' will be applied to account for changes between the Preliminary Determination and the Substitute Determination. These 'true-up' adjustments are set out by transitional clauses 11.60.4(d) and (e) of the NER.

These transitional arrangements modify the usual timeline for the making of the AER's decisions regarding our revenue controls. In turn, this modifies the timeline for the submission of our Regulatory Proposal, revised Regulatory Proposal, and other documents associated with the revenue determination process. We will address this issue by submitting the required proposals in accordance with the transitional provisions.

[7] There are only three non-prescribed connection points in the regulatory control period 2015-20.