

# ATTACHMENT 9.4

## TYPE 5 & 6 METERING SERVICES

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## 1. PURPOSE

The purpose of this paper is to present to the Australian Energy Regulator (AER) Essential Energy's response to the issues raised by the AER in the *Draft Decision Essential Energy Distribution Determination (2015-16 to 2018-19) – Attachment 16: Alternate control services*, in particular those issues related to metering services.

This report does not respond in detail to the following issues identified by the AER:

- > Change in roll forward model for RAB (Attachment 5.1)
- > Efficiency of labour costs (Attachment 7.5)

## 2. SUMMARY

Issues raised by the AER regarding Essential Energy's metering services proposal and Essential Energy's response are highlighted in the table 2-1 below:

**Table 2-1: AER issues and Essential Energy's response**

AER issue	Summary of AER's reasons and findings	Essential Energy's response
Exit fee	<p>The AER believes the exit fee will create a regulatory barrier to competitive entry.</p> <p>AER revised classification of residual metering costs to be standard control and recovered through network tariffs.</p> <p>Administrative costs will continue to be classified as alternate control, however were not justified by Essential Energy.</p>	<p>Essential Energy has accepted the AER's change in classification of residual metering costs, with these costs now to be recovered through standard control. We do not accept the AER's tolerance limit for the metering component of the b-factor adjustment but instead believe that side constraints and treatment of the unders and overs account should be applied to the total DUoS amount as outlined in Chapter 10 of our revised proposal.</p> <p>Essential Energy has demonstrated incremental administrative costs associated with a customer moving from type 5 &amp; 6 regulated metering to an alternate metering service provider.</p> <p>Essential Energy continues to propose an exit fee to cover the administrative component only, which is in line with the independent advice obtained by the AER.</p>
Capital expenditure	<p>Unit costs were not considered to be reflective of the lowest cost meter available, considering Networks NSW's buying power.</p>	<p>Essential Energy rejects the AER's calculations and has resubmitted capital expenditure based on unit costs within the substantive regulatory proposal.</p>
Operating expenditure	<p>Base operating expenditure should be lower than the amount Essential Energy used to develop its forecast.</p> <p>Benchmarking completed against Ergon, with average cost per customer for Ergon used as an efficient base for Essential Energy.</p>	<p>When looking at the comparisons between Essential Energy and Ergon, it would appear reasonable that Essential Energy's efficient operating costs would be marginally higher than that of Ergon Energy.</p> <p>Essential Energy has a lower customer density, almost double the number of customers on long rural feeders, and a higher number of meters per customer.</p>
Up-front meter charges	<p>The AER found material unit costs did not reasonably reflect the efficient costs of a prudent operator.</p> <p>Non-material unit costs were considered to be outside of benchmarking maximum set by Marsden Jacobs.</p>	<p>Essential Energy considers that an efficient annualised cost has been achieved for all new metering equipment through the business's metering equipment procurement strategy.</p> <p>Non-material unit costs have been applied, consistent with the AER-approved CAM.</p>

Opening RAB value	Value had to be recalculated due to changes in the roll forward model for standard control.	Essential Energy does not accept the change to the roll forward model and has not applied the revisions to the opening RAB value in the revised proposal.
Accelerated depreciation	The AER does not consider this accelerated depreciation to be efficient.	Essential Energy reviewed the proposed depreciation model for metering equipment and accepted the AER's revised remaining asset life of 19.7 years with depreciation calculated on a straight-line basis. New meters will be depreciated over standard life of 15 years.

### 3. BACKGROUND

In its regulatory submission, Essential Energy proposed charges for metering services that were transparent and cost-reflective, while the business transitions to an environment of increased competition. Charges were based on the meter service a customer was receiving. To develop cost-reflective charges, historical costs were examined to determine the drivers of metering costs, which include recovering the costs of existing meters and new meters, as well as operating and replacement costs.

The AER did not accept Essential Energy's proposed metering charges, believing costs were overstated and exit fees were a barrier to competition. Specifically the AER stated:

- *To avoid creating a regulatory barrier to competitive entry, we do not accept Essential Energy's proposal to charge an exit fee to leaving customers to recover residual metering costs. Instead residual metering costs will be classified as a standard control service and recovered from the general network customer base<sup>1</sup>.*
- *We accept Essential Energy's proposal to recover the capital costs of new/upgraded connections as upfront payments... We also accept its proposal to have a separate annual charge for new and upgraded customers, in recognition they have already paid for the capital costs for their metering installations<sup>2</sup>.*
- *We do not consider Essential Energy's forecast material unit costs to reasonably reflect the efficient costs of achieving the capital expenditure objectives or the costs of a prudent operator<sup>3</sup>.*
- *We accept a building block approach to setting charges but do not accept the following components of the Essential Energy proposal:*
  - *The capital and operating expenditure*
  - *The opening metering RAB<sup>4</sup>.*
- *We do not accept the remaining and standard asset lives proposed by Essential Energy; we do not consider that this accelerated depreciation is efficient<sup>5</sup>.*

We have reviewed our charges to ensure they reflect the latest information available and represent a cost-reflective and efficient outcome. Metering services overhead rates have been updated to reflect efficiency outcomes consistent with Standard Control Services and Essential Energy's AER approved CAM.

The revised charges are provided as attachment 9.7 to this proposal.

<sup>1</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 29

<sup>2</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 30

<sup>3</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 38

<sup>4</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 37

<sup>5</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 43

## 4. DISCUSSION

In this section the specific issues raised by the AER are discussed:

- > Exit fee;
- > Up front meter charges;
- > Annual metering charge, including operating, capital expenditure and RAB.

Essential Energy will also discuss the control mechanism proposed for metering.

### 4.1. Exit fee

The Australian Energy Market Commission (AEMC) is currently in the process of formulating a rule change associated with the increased competition in metering, which will help facilitate a market led roll-out of advanced metering. The AEMC provided that an appropriate, clearly defined and transparent exit fee for accumulation or manually read interval meters would be expected to encourage competition and more efficient investment in advanced metering<sup>6</sup>. In preparation for these regulatory changes, Essential Energy proposed a metering exit fee comprising the residual meter cost and administrative costs associated with the transfer. The AER has rejected both components.

#### *Residual metering costs*

As discussed above, the AER rejected Essential Energy's proposed approach and charges on the basis that the exit fee (including recovery of residual asset cost and administrative charge) was anti-competitive. The AER has proposed that DNSPs be allowed to recoup the stranded costs created by competition at the time a customer obtains an alternate metering service provider, through the standard control mechanism. The existing metering asset base would be recovered from annual metering charges under Alternative Control. However, if the customer chose to have a third party meter replace the existing meter, an amount (equal to the residual value of the asset) would be recovered via an adjustment to standard control services. In its draft decision, the AER stated:

*We reject Essential Energy's proposed exit fee. Specifically, we do not accept that Essential Energy should recover residual metering costs through an exit fee. Our alternative is to classify residual metering costs (the metering RAB component of annual charges that the customer would have paid had they remained a regulated metering customer) as standard control service and recover these through network tariffs<sup>7</sup>.*

Essential Energy acknowledges this change in classification will assist in removing financial barriers to competition while still providing cost recovery options for LNSPs. This change in classification will, however, result in further cross subsidies, with the residual value being recovered from all customers rather than the customer exiting. Where churn volume is small, these cross subsidies will be insignificant, however Essential Energy is concerned about the effect on pricing should churn volume increase significantly. The AER has recognised this risk and has placed a tolerance limit, which cap the amount of additional revenue that can be added to DUoS tariffs on an annual basis.<sup>8</sup>

The AER has determined that Essential Energy will implement tolerance limits to the recovery of residual metering costs. If the residual metering asset costs under/over recovery compared to the annual revenue requirement (ARR) for year t are:

- > less than two per cent, the residual metering assets costs under/over recovery will be cleared within one regulatory year

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<sup>6</sup> AEMC, Consultation Paper, National Electricity Amendment (Expanding Competition in Metering and Related Services) Rule 2014 and National Energy Retail Amendment (Expanding Competition in Metering and Related Services) Rule 2014, 17 April 2014, pg 51

<sup>7</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 30

<sup>8</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 46

- > greater than two per cent, the residual metering assets costs under/over recovery will be recovered in the remainder of the regulatory control period.<sup>9</sup>

Essential Energy supports the facilitation of competition in metering services, provided the AER has satisfied itself that this is not creating an artificially competitive market and is a pragmatic, compliant and simple solution. As such, Essential Energy has revised its proposal to adopt the AER’s approach, excluding residual asset costs from the proposed ‘meter exit fee’. However, as outlined in Chapter 10 of the revised regulatory proposal, Essential Energy does not accept the AER’s tolerance limit for the metering component of the b-factor adjustment. It is an efficient, approved cost that would form part of Essential Energy’s standard control RAB, so it would be inappropriate to deny the recovery of this revenue if it were to exceed the two per cent limit.

The timeline associated with the AEMC rule change process may result in material adjustments late in the 2014-19 regulatory control period. It is proposed that all DUoS amounts be subject to one side constraint and one rule for the treatment of any under or over recovery, including the recovery of stranded meter asset costs added to the standard control RAB.

### Administration costs

Regarding the administrative component of the proposed exit fee, the AER has accepted the principle of a fee, specifically ‘meter transfers’, and has maintained the classification and control mechanism as an alternate control service. However, the AER rejected Essential Energy’s proposed fee:

*We are satisfied the service ‘meter transfers’ should be classified as an alternative control service and recovered through an exit fee.<sup>10</sup>*

and

*We accept in principle that Essential Energy should be allowed charge an exit fee based on incremental administrative costs incurred to process a customer transfer. However, as Essential Energy did not adequately demonstrate they will incur incremental administrative costs, we are led to reject an exit fee based on administrative costs<sup>11</sup>.*

In response to the matters raised by the AER, Essential Energy has reviewed its proposed administration fee and revised it. Specifically, the business has sought to better understand and justify the activities involved in transferring a metering customer and the incremental costs involved. As such, Essential Energy’s revised metering transfer cost is as follows:

**Table 4-1: Meter transfer - exit fee price build up**

Cost Component	Time	Cost per meter \$2013/14
Receive and validate meter change paperwork	2 mins	\$ 3.41
Update billing system with meter removal and the new metering details (for the non-Essential Energy asset)	8 mins	\$ 13.64
Remove meter from MDP system and make basic data streams inactive	10 mins	\$ 17.05
Obtain final reads and enter in MDP system to send NEM13 file to market and billing	2 mins	\$ 3.41

<sup>9</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 14: Control mechanisms for standard control services, November 2014, pg 11

<sup>10</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 13: Classification of distribution services, November 2014, pg 11

<sup>11</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 47

Cost Component	Time	Cost per meter \$2013/14
Configure the billing system for interval data streams	5 mins	\$ 8.53
Cost of meter disposal		\$ 1.63
<b>Meter transfer - exit fee (per meter)</b>	27 mins	<b>\$ 47.68</b>

These prices are subject to CPI changes and will presumably escalate each year. They represent the incremental costs that will be incurred by Essential Energy for all metering services that churn to alternate metering providers. Essential Energy has estimated these costs using historical data that is available from existing meter transfers occurring where sites move from a type 6 to a type 4 contestable metered site. As the sites are moving from a basic metered site to an interval site, the set-up process is slightly longer than for a basic-to-basic meter change to allow for the configuration of interval data streams.

Refer to the type 5 & 6 metering services model attachment 9.5 for further detail.

In setting the classification of services, the AER must have regard to section 6.2.2(c) of the NER:

- (c) The AER must, in classifying a direct control service as a standard control service or an alternative control service, have regard to:*
- (1) the potential for development of competition in the relevant market and how the classification might influence that potential; and*
  - (2) the possible effects of the classification on administrative costs of the AER, the Distribution Network Service Provider and users or potential users; and*
  - (3) the regulatory approach (if any) applicable to the relevant service immediately before the commencement of the distribution determination for which the classification is made; and*
  - (4) the desirability of a consistent regulatory approach to similar services (both within and beyond the relevant jurisdiction); and*
  - (5) the extent the costs of providing the relevant service are directly attributable to the person to whom the service is provided; and*
  - (6) any other relevant factor.*

Essential Energy acknowledges the existence of an exit fee may impact on the development of competition in the metering market, however the AER also needs to consider the removal of cross-subsidisation where a service is able to be directly attributed to the person to whom the service is provided. Quite clearly meter transfer services provided by Essential Energy are in direct response to the decision of a customer to move to contestable metering; therefore, those costs should be attributed to transferring customers and not borne by all customers.

In addition to Essential Energy's revised position, it is also noted that the AER's consultant, Marsden Jacob, provided a benchmark 'meter transfer fee'. This recommendation was not adopted by the AER in its draft decision, despite the report being heavily relied upon for all remaining ancillary network services fees. Marsden Jacob noted:

*Marsden Jacob recommends that the total labour rates which apply to administration processing of meter exits should be capped at \$89.06. The total labour rate proposed is consistent with market salary rates for administration and processing positions and includes standard on-costs and overheads of 50%. This rate is consistent with the benchmarked labour rates proposed by Marsden Jacob for Ancillary Network Services (refer to 1.1.4).*

*We also recommend that the time taken to perform each exit should, on average, be capped at 0.40 hours. In making the recommendation, Marsden Jacob consider the time taken to perform other metering services including special meter reads, disconnection services and meter equipment tests. Times proposed by the NSW and ACT distribution businesses for the current determination process were considered as well as the accepted time taken for back-office aspects of services in the most recent Victorian regulatory determination. As the exit process is yet to be fully defined and the actual time needed to process changes*



*is unknown, Marsden Jacob's recommendation is to accept the lower rate proposed by the two distribution businesses at this point.*

*Marsden Jacob notes that a SA Power Network's current exit fee for customers consuming above 100MWh transitioning from type 6 ACS metering service into the competitive market includes an administration component of around \$60.00 (\$2010)<sup>12</sup>.*

Essential Energy considers it would be unreasonable for the final decision to set the fee at \$0 in light of the further justification provided to support the revised fee and the benchmark rate provided by the AER's consultant.

Essential Energy has revised its metering services list of charges to adopt the decision to remove the residual value of meters from the proposed exit fee. The fee now reflects the incremental administration and disposal costs associated with a customer switching to an alternate metering service provider.

#### **4.2. Upfront meter charges**

In determining the reasonableness of proposed charges for new or upgraded connections, referred to as the up-front meter charge, the AER analysed Essential Energy's unit cost.

The AER rejected the up-front meter charges proposed by Essential Energy on the basis they were above the lowest rates identified by the AER's consultant, Marsden Jacob. Essential Energy has not revised its regulatory proposal to adopt the AER's alternative charges; however charges have been reviewed to ensure they represent a comprehensive and accurate list of available meters based on the most recent market information.

#### **Material unit costs**

Essential Energy does not consider the AER decision reasonable as it adopts the lowest cost meter in each range provided by Marsden Jacob. Marsden Jacob has not specified meter models or manufacturers, therefore it is unlikely Essential Energy can achieve these charges without sufficient detail to know which meters should be procured. Furthermore, Essential Energy has not been able to assess whether the low cost meters referred to by Marsden Jacob are of sufficient quality or reliability.

The acquisition of metering equipment is a long term decision, as it typically has an asset life up to 15 years. Achieving the lowest annualised cost for provision of the metering services requires a balance of capital and operating expenditure. The procurement of the lowest cost metering equipment will often require a greater level of operational expenditure to support early life failures and a greater failure rate over time. The higher cost metering equipment often has better quality components, resulting in lower ongoing maintenance costs. Determining the optimal cost position requires an accurate forecast of future failure rates. This is often only possible once a history of asset operation and failure has been established.

A further consideration in the selection of metering equipment is the mounting hole pattern of the device. The preference is to procure metering equipment for use within maintenance programs that have a similar mounting pattern to existing installed devices, thereby providing a lower and more efficient total replacement cost. Essential Energy has a high percentage of asbestos meter boards in its network. Maintenance activities that require drilling of an asbestos board require specific procedures, resulting in increased time and associated labour costs. Essential Energy estimates that where drilling is required on an asbestos board, an additional seven to 10 minutes is added to the meter replacement activities; equating to \$14 to \$21 in additional labour costs. These costs must be considered in determining the overall efficient costs of metering equipment.

Essential Energy considers that an efficient annualised cost has been achieved for all new metering equipment through the business's metering equipment procurement strategy, including economy of scale benefits achieved through joint procurement across Networks NSW. Essential Energy believes the economies of scale proposed by the AER are not realistic within its operating environment, given the volume of meters procured in NSW each year. The comparison to Victorian bulk procurement arrangements is irrelevant considering the difference in the volume of meters procured per annum (approximately 110,000 per year in NSW versus nearly one million meters procured per year in Victoria during the recent smart meter roll-out).

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<sup>12</sup> Marsden Jacob Associates, Provision of advice in relation to Alternate Control Services, 20 October 2014, pg 20



Ultimately, the re-classification of metering is designed to facilitate customer choice and a movement towards competition. Essential Energy considers customers should be provided a full range of meter models to select from when making their decision. While it is reasonable to provide customers the lowest cost option available, those who value quality, lower annual costs or have other priorities, should be afforded choice. Provided the charges set by the AER are cost reflective, this decision should be left to the customer.

### ***Non-material unit costs***

In making its draft decision, the AER has also reviewed the non-material costs associated with meters, where non-material unit costs refer to the expenditure required to install, handle and manage the logistics associated with putting a new meter into service<sup>13</sup>. This definition differs slightly from Marsden Jacobs's - non-material costs comprising meter issuance, acceptance testing and other meter handling costs<sup>14</sup>. Non-material costs proposed by Essential Energy do not include costs associated with meter installation, as this work is presently performed by ASPs and funded directly by customers.

Essential Energy's proposed non-material unit costs were determined by applying the appropriate stores on-costs and overheads. These are applied to the meter charge on a percentage basis consistent with Essential Energy's Cost Allocation Methodology (CAM) approved by the AER in May 2014.

*Marsden Jacob has not considered the reasonableness of applying a percentage rate rather than a flat dollar fee and as such, we do not recommend any changes to the methodology adopted by Essential Energy in proposing non-material costs for new meters. However we recommend the average weighted per meter fees should equate to a maximum of \$25.00 per meter.*

*We note that Essential's proposed non-material costs include provision for overheads. In adopting a recommended average weighted cost of \$25.00 per meter, we also recommend the treatment of overheads for this service should first be reviewed for consistency with Essential's Cost Allocation Methodology and the finding of that investigation be considered.<sup>15</sup>*

The AER does not indicate whether it has considered Marsden Jacobs' recommendation in full and reviewed Essential Energy's non-material cost allocation in accordance with the CAM. Essential Energy has been consistent in its application of the CAM and applied stores on-costs and overheads on a percentage basis to the base meter purchase costs.

Essential Energy has resubmitted its updated price list for up-front metering charges reflecting the alteration to overheads; incorporating efficiency adjustments consistent with standard control services.

### **4.3. Annual metering fee**

In determining Essential Energy's annual metering fee, the AER assessed Essential Energy's proposed capital and operating expenditure building blocks and opening metering regulatory asset base.

### ***Capital costs***

In developing alternate annual metering charges, the AER reduced Essential Energy's proposed metering capital expenditure program. Specifically, the AER stated:

*We accept \$50.3 million in capital expenditure for the 2014-15 and 2015-19 regulatory control periods and substitute that amount for Essential Energy's proposed \$51.5 million (\$2014/15).<sup>16</sup>*

<sup>13</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 39

<sup>14</sup> Marsden Jacob Associates, Provision of advice in relation to Alternate Control Services, 20 October 2014, pg 17

<sup>15</sup> Marsden Jacob Associates, Provision of advice in relation to Alternate Control Services, 20 October 2014, pg 19

<sup>16</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 37

In assessing the proposed capital expenditure, the AER reviewed 'unit costs' and 'volume forecasts'. The AER has generally accepted the proposed volume forecasts provided by Essential Energy.

*We accept Essential Energy's new or upgraded connections for 2014-15 and the distribution business' forecast replacement volumes.<sup>17</sup>*

The AER has reduced proposed capital costs but has not clearly articulated what this reduction relates to. It would appear this reduction is based on the revised unit costs for metering hardware and non-material costs as determined within the Marsden Jacobs report. As mentioned regarding up-front meter charges, Essential Energy does not accept the cheapest meter provides the lowest total cost for new and replacement activities.

The AER has substituted the lowest end of the determined market rate range, as provided by Marsden Jacobs, as the prudent hardware price and adjusted the forecast capital expenditure accordingly. This is based on the assumption that ongoing procurement improvements by NNSW will lead to the lowest market price. While price is one determining factor in Essential Energy's procurement process, this needs to be balanced with the ongoing operating costs associated with the metering equipment. Essential Energy considers the efficient annualised cost for all new metering equipment through its metering equipment procurement strategy, in an effort to procure metering equipment at the lowest overall economic cost to the business and customers.

Essential Energy rejects the use of the lowest cost meter as being the most efficient overall economic cost; as such Essential Energy has submitted a revised regulatory proposal using meter procurement rates as per the original proposal.

A minor change has been made to Essential Energy's revised regulatory proposal to include a correction of unit rates for single phase accumulation meter purchases within the metering model<sup>18</sup>.

## Operating costs

In addition to the reductions to Essential Energy's proposed capital costs, the AER has made significant reductions to metering operating expenditure in establishing alternative charges. The AER has primarily relied on benchmarking to reject and substitute Essential Energy's proposed operating expenditure, specifically noting:

*We approve \$120.2 million in operating expenditure for annual metering services and substitute that amount for Essential Energy's proposed \$131.3 million (\$2014–15). This is an 8 per cent reduction from the proposed amount. However, our draft decision is based on an efficiency adjustment, rather than step change for special meter reads as Essential Energy proposed.<sup>19</sup>*

The AER recognises that Essential Energy's proposed operating expenditure per customer for the 2014-15 and 2015-19 regulatory control periods performs well against historical results, but was concerned that most of this reduction related to the step change for special meter reads, rather than efficiency forecasts. The AER has therefore made an efficiency adjustment based on benchmarking results to the base operating expenditure.

*Our benchmarking results shows Essential Energy's proposed operating expenditure to be overstated. To more reasonably reflect a relatively more efficient business running a network with Essential Energy's characteristics, we substitute the proposed base operating expenditure with an amount equal to Ergon Energy's per customer spend<sup>20</sup>.*

Essential Energy proposed \$35 per customer, but the AER has substituted Essential Energy's proposed base expenditure with an amount equal to Ergon Energy's per customer spend, being \$32 per customer. Ergon Energy was considered to be a relevant comparator for Essential Energy as it has a similar customer density.

<sup>17</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 39

<sup>18</sup> Refer to response to information request AER Essential 031\_Metering Costs provided on 16 October 2014

<sup>19</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 40

<sup>20</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 42

Table 4-2 below provides a relevant comparison between Essential Energy and Ergon Energy. When looking at the comparisons below, it would appear reasonable that Essential Energy's efficient operating costs would be marginally higher than that of Ergon Energy:

- > Essential Energy has a lower density of customers per kilometre;
- > Essential Energy has on average 1.86 meters per customer compared to 1.72 meters per Ergon customer;
- > Ergon has 10% more customers residing within an urban environment, while Essential Energy has nearly double the number of customers residing on a long rural feeder.

**Table 4-2: Essential Energy – Ergon Energy Comparison<sup>21</sup>**

	Essential Energy	Ergon Energy	Comparison
Customer Density	4.671	5.023	-7%
Customer Numbers	844,244	710,431	15.8%
Urban	196,664 / 23.3%	238,762 / 33.6%	-10.3%
Short Rural	513,663 / 60.8%	389,329 / 54.8%	6%
Long Rural	133,917 / 15.9%	74,368 / 10.5%	5.4%
Meter Numbers	1,567,809	1,222,528	22%

Most metering-related services are performed at a customer's premises, for example meter reading and meter maintenance. Metering costs are inclusive of the time taken to attend the site and are highly influenced by the location of customers.

Essential Energy had provided for a step change in its proposal, associated with metering services that are now classified as ancillary network services. Most of this step change related to the removal of special meter reads. The AER has applied reductions based on the efficiency adjustment and is seeking to make further adjustments during the final determination.

*Our substitute is marginally less than Essential Energy's proposal. However, our cut based on a benchmarking efficiency adjustment rather than Essential Energy's proposed step change. Our final decision which will include the step change for classification changes will therefore further reduce Essential Energy's metering operating expenditure<sup>22</sup>.*

Essential Energy is concerned the AER is seeking to apply further reductions to Essential Energy's metering expenditure by applying a step change for classification changes in the final determination. Essential Energy has no visibility of the quantum of the step change the AER will seek to apply. As it will be applied in the final determination, Essential Energy has had no opportunity to review and provide comment within the revised regulatory proposal.

<sup>21</sup> Source: AER published 'Essential Energy 2006-13 - Economic Benchmarking RIN - financial and non-financial information' and 'Ergon 2006-13 - Economic Benchmarking RIN - financial and non-financial information' and 'Ergon Energy 2012-13 - Annual Reporting RIN - non financial information'

<sup>22</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 43

## Regulatory asset base

The AER draft decision has revised the opening meter RAB value to \$115.1 million.

*We do not accept the opening metering RAB as at 1 July 2014 of \$118.2 million (\$nominal) as separated by Essential Energy from the RAB for standard control services (SCS). We have determined an opening metering RAB of \$115.1 million (\$nominal) instead<sup>23</sup>.*

This adjustment is associated with changes in the roll forward model for standard control services as discussed in Chapter 5 of the revised regulatory proposal. The AER made adjustments to Essential Energy's proposed value of the RAB as at 1 July 2014 (opening RAB values). Essential Energy does not agree with these adjustments and has not incorporated the AER's opening RAB values in the calculation of metering charges. It is noted, however, that the metering RAB value has decreased as a result of capital expenditure in 2013/14 being lower than forecast in the original proposal

The AER also rejected Essential Energy's proposal for accelerated depreciation of the metering RAB.

*We do not accept the remaining and standard asset lives proposed by Essential Energy... We do not consider that this accelerated depreciation is efficient. It is unlikely that all meters will be provided by alternate service providers within 7 years<sup>24</sup>.*

Essential Energy proposed accelerated depreciation to remove legacy assets from the metering RAB as quickly as practical with the introduction of metering contestability. Essential Energy is unable to forecast the amount of churn that may occur due to installation of contestable meters on its distribution network over the 2014-19 regulatory control period, however it is expected that a large proportion of existing metering assets will remain in place and operational at the end of the period. As such, Essential Energy has reviewed its proposed depreciation model for metering equipment and has accepted the AER's revised remaining useful life of 19.7 years with straight-line depreciation to apply. New meters will be depreciated over the standard life of 15 years.

### 4.4. Control mechanism for metering

The AER draft decision applies a price cap for the form of control for metering services. Charges will be set for each year of the regulatory period, with the charges adjusted annually by CPI and an X factor. Essential Energy notes the AER has not allowed for an X factor adjustment in outer years as the X factor has been set to zero<sup>25</sup>. Essential Energy agree with this approach as it is assumed this is due to wage and cost escalators already being included in the price build-up for metering charges over the regulatory period, as some of these costs are capital and form part of the metering RAB.

Essential Energy notes that an X factor has been allowed in the draft decision for ancillary network service charges, which is inconsistent with the control mechanism for metering. Cost escalation has already been included for these metering charges to ensure the correct amount is included in the metering RAB.

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<sup>23</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 43

<sup>24</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 43

<sup>25</sup> AER, Draft decision Essential Energy distribution determination 2015-16 to 2018-19 Attachment 16: Alternative control services, November 2014, pg 48