

Attachment 11: Control mechanisms

Regulatory proposal for the ACT electricity distribution network 2019–24
January 2018

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11.1. Introduction

In this attachment, Evoenergy outlines its proposal relating to the control mechanisms for Standard Control Services (SCS). This includes the treatment of Distribution Use of System (DUOS), Designated Pricing Proposal Charges and Jurisdictional Scheme amounts. Evoenergy's proposed pricing methodology for transmission services is provided in Appendix 11.1. The proposal and requirements for Alternative Control Services are outlined in Attachment 14 (Alternative Control Services).

Evoenergy's proposal for SCS control mechanisms is consistent with the National Electricity Objective and the revenue and pricing principles in the National Electricity Rules (Rules). The proposal is designed to deliver long-term benefits to customers by encouraging efficient supply and use of current network services, and by providing cost-reflective price signals to guide future decisions.

11.2. Regulatory requirements

The Australian Energy Regulator's (AER's) constituent decisions are set out in clause 6.12.1 of the Rules. The following constituent decisions are relevant for SCS control mechanisms.

- A decision on the form of the control mechanisms (including the X-factor) for SCS (to be in accordance with the AER's Framework and Approach paper) and on the formulae that give effect to those control mechanisms (clause 6.12.1(11)).
- A decision on how compliance with a relevant control mechanism is to be demonstrated (clause 6.12.1(13)).
- A decision on how the Distribution Network Service Provider (DNSP) is to report to the AER on its recovery of Designated Pricing Proposal Charges for each regulatory year of the regulatory control period and on the adjustments to be made to subsequent pricing proposals to account for over or under recovery of those charges (clause 6.12.1(19)).
- A decision on how the DNSP is to report to the AER on its recovery of Jurisdictional Scheme amounts for each regulatory year of the regulatory control period and on the adjustments to be made to subsequent pricing proposals to account for over or under recovery of those amounts. A decision under subparagraph (20) must be made in relation to each Jurisdictional Scheme under which the DNSP has Jurisdictional Scheme obligations at the time the decision is made (clause 6.12.1(20)).

11.3. The control mechanism for SCS

In its Framework and Approach paper, the AER decided that a revenue cap form of control will apply to Evoenergy's distribution services for the 2019–24 regulatory control period.¹ This is a departure from the 2014–19 regulatory control period, and previous

¹ AER 2017, Framework and Approach—ActewAGL, July, p. 11.

periods, where an average revenue cap form of control has been applied to Evoenergy's distribution services.

The AER's proposed approach to the formulae that give effect to the control mechanism for distribution services is also set out in the Framework and Approach paper. The AER must include the proposed formulae in its distribution determination, unless it considers that unforeseen circumstances justify departing from the formula set out in the Framework and Approach paper.²

As prescribed in the Framework and Approach paper, the proposed revenue cap formula for distribution services in the 2019–24 regulatory control period is:

$$TAR_t \geq \sum_{i=1}^n \sum_{j=1}^m p_t^{ij} q_t^{ij} \quad i = 1, \dots, n \text{ and } j = 1, \dots, m \text{ and } t = 1, 2, \dots, 5$$

$$2. \quad TAR_t = AAR_t + I_t + B_t + C_t \quad t = 1, 2, \dots, 5$$

$$3. \quad AAR_t = AR_t \times (1 + S_t) \quad t = 1$$

$$4. \quad AAR_t = AAR_{t-1} \times (1 + \Delta CPI_t) \times (1 - X_t) \times (1 + S_t) \quad t = 2, \dots, 5$$

where:

TAR_t is the total allowable revenue in year t.

p_t^{ij} is the price of component 'j' of tariff 'i' in year t.

q_t^{ij} is the forecast quantity of component 'j' of tariff 'i' in year t.

t is the regulatory year.

AR_t is the annual smoothed revenue requirement in the post-tax revenue model (PTRM) for year t.

AAR_t is the adjusted annual smoothed revenue requirement for year t.

I_t is the sum of incentive scheme adjustments in year t. To be decided in the distribution determination.

B_t is the sum of annual adjustment factors in year t. Likely to incorporate but not limited to adjustments for the overs and unders account. To be decided in the distribution determination.

C_t is the sum of approved cost pass through amounts (positive or negative) with respect to regulatory year t, as determined by the AER. It will also include any end-of-period adjustments in year t. To be decided in the distribution determination.

² Rules, clause 6.12.3(c1).

S_t is the S-factor for regulatory year t.³ As it currently stands, the S-factor will incorporate any adjustments required due to the application of the AER's STPIS.⁴

ΔCPI_t is the annual percentage change in the Australian Bureau of Statistics (ABS) Consumer Price Index (CPI) All Groups, Weighted Average of Eight Capital Cities,⁵ from the December quarter in year t-2 to the December quarter in year t-1, calculated using the following method:

the ABS CPI All Groups, Weighted Average of Eight Capital Cities, for the December quarter in regulatory year t-1

divided by

the ABS CPI All Groups, Weighted Average of Eight Capital Cities, for the December quarter in regulatory year t-2

minus one.

For example, for 2020-21, year t-2 is the December quarter 2018 and year t-1 is the December quarter 2019.

X_t is the X-factor in year t, incorporating annual adjustments to the PTRM for the trailing cost of debt where necessary. To be decided in the distribution determination.

Evoenergy does not propose any changes to the formulae for SCS proposed by the AER in its Framework and Approach paper.

11.4. Compliance with the control mechanism

To demonstrate compliance with the AER's revenue cap control mechanism, Evoenergy proposes to report on revenue amounts and make adjustments to its annual pricing proposal for over and under recovery.

As part of the annual pricing proposal for each regulatory year, Evoenergy proposes to provide the following amounts for the most recently completed regulatory year:

1. the opening balance for each year;
2. the interest accrued on the opening balance for each year, calculated at the semi-annual interest rate;
3. the value of any approved pass throughs;

³ The meaning for year 't' under the price control formula is different to that in Appendix C of Service Target Performance Incentive Scheme (STPIS). Year 't+1' in Appendix C of STPIS is equivalent to year 't' in the price control formula of this decision.

⁴ AER, Electricity distribution network service providers—service target performance incentive scheme, 1 November 2009.

⁵ If the ABS does not or ceases to publish the index, then CPI will mean an index which the AER considers is the best available alternative index.

4. the amount representing the revenue recovered from distribution service charges applied in respect of that year;
5. an adjustment to the net amount in item 3 by six months of interest, accrued at the approved nominal rate of return; and
6. a summation of the above amounts to derive the closing balance for each year.

Table 11.1 Example calculation of Evoenergy’s DUOS overs and unders account

	2019/20 Estimate	2020/21 Forecast	2021/22 Forecast
Revenue from DUOS charges	145,000	150,000	157,845
Total allowable revenue	150,000	148,000	154,000
Incentive schemes	50	20	0
Adjustment factors	50	20	0
Cost pass throughs	50	20	0
STPIS	50	20	0
Total distribution-related payments	150,200	148,080	154,000
Over (under) recovery for the financial year	-5,200	1,920	3,845
Overs and unders account			
Annual rate of interest applicable to balances	6.48%	6.38%	6.35%
Semi-annual interest rate	3.19%	3.14%	3.13%
Opening balance	0	-5,366	-3,728
Interest on opening balance	0	-343	-237
Over/under recovery for financial year	-5,200	1,920	3,845
Interest on over/under recovery	-166	60	120
Closing balance	-5,366	-3,728	0

Note – Figures in Table 11.1 are for the sole purpose of demonstrating the theoretical operation of the DUOS unders and overs account and are not based on figures from Evoenergy’s network pricing model.

In practice, the proposed overs and unders account for distribution (Table 11.1) is consistent with the overs and unders account Evoenergy operates for designated pricing proposal charges in the 2014–19 regulatory period.

For each year after the first year of the regulatory control period, side constraints will apply to the revenue to be raised from each tariff class.⁶ In accordance with clause 6.18.6 of the Rules, the permissible percentage increase is the greater of CPI—X plus 2 per cent or CPI + 2 per cent. Recovery of revenue to accommodate cost pass throughs and pass through of Designated Pricing Proposal Charges and Jurisdictional Scheme amounts is disregarded when deciding whether the permissible percentage has been exceeded.

11.5. Designated Pricing Proposal Charges

Designated Pricing Proposal Charges are defined in Chapter 10 of the Rules and are any of the following services:

- charges for designated pricing proposal services;
- avoided Customer Transmission Use of System (TUOS) charges;
- charges for distribution services provided by another DNSP, but only to the extent those charges comprise:
 - charges incurred by that DNSP for designated pricing proposal services; or
 - charges for Standard Control Services;
- charges or payments specified in Clause 11.39.

In this context, designated pricing proposal services refers to any of the following services:

- prescribed exit services;
- prescribed common transmission services; and
- prescribed TUOS services.

Evoenergy is satisfied with the current approach and cannot foresee any problems associated with this approach continuing in the 2019–24 regulatory control period. This approach is consistent with Clause 6.18.7 of the Rules. An example of this approach is depicted in Table 11.2.

⁶ Under the Rules, the side constraint only applies to pricing in the second and subsequent regulatory years of the regulatory control period. This is because Clause 6.18.6(b) provides that the expected weighted average revenue to be raised from a tariff class for a particular regulatory year of a regulatory control period must not exceed the corresponding expected weighted average revenue for the preceding regulatory year in that regulatory control period by more than the permissible percentage. As the side constraint is calculated with reference to the expected weighted average revenue in the preceding year in the regulatory control period, the side constraint cannot apply in the first year of a regulatory control period.

Table 11.2 Indicative calculation of Evoenergy’s TUOS overs and unders account

	2015/16 Actual	2016/17 Estimate	2017/18 Forecast
Revenue from TUOS charges	61,776	61,788	31,639
Evoenergy Dual Function Asset Revenue Cap	24,102	24,352	24,609
Net transmission charges paid to TNSPs	34,535	22,709	26,917
Avoided TUOS payments	62	62	62
Inter-DNSP payments	0	0	0
Total transmission-related payments	58,699	47,123	51,588
Over (under) recovery for the financial year	3,077	14,664	-19,949
Overs and unders account			
Annual rate of interest applicable to balances	6.38%	6.35%	6.30%
Semi-annual interest rate	3.14%	3.13%	3.10%
Opening balance	-16	3,157	18,480
Interest on opening balance	-1	201	1,163
Over/under recovery for financial year	3,077	14,664	-19,949
Interest on over/under recovery	97	459	-618
Closing balance	3,157	18,480	-924

11.6. Jurisdictional Scheme amounts

Evoenergy currently administers the collection of revenue associated with four Australian Capital Territory (ACT) jurisdictional schemes, the cost of which is not included in the operating expenditure allowance, but recovered as separate charges in addition to DUOS, TUOS and metering. Applicable jurisdictional schemes in the ACT are:

- Feed-in Tariffs (small and medium scale);
- Feed-in Tariffs (large scale);

- Utilities Network Facilities Tax; and
- Energy Industry Levy.

The Jurisdictional Scheme arrangements in the Rules include a provision for DNSPs to request the AER to determine that a scheme is a Jurisdictional Scheme (Clause 6.6.1A(b)).

Evoenergy's proposal on the manner in which Evoenergy is to report on Jurisdictional Scheme amounts and to make adjustments to its annual pricing proposal for over and under recovery for the 2019–24 regulatory control period is identical to what is in place in the 2014–19 regulatory control period (Table 11.3).

As part of the annual pricing proposal for each regulatory year, Evoenergy proposes to provide the following amounts for the most recently completed regulatory year:

1. the opening balance for each year;
2. the interest accrued on the opening balance for each year, calculated at the rate of post-tax nominal rate of return as approved by the AER in its distribution determination;
3. the value of any approved pass throughs;
4. the amount representing the revenue recovered from distribution service charges applied in respect of that year;
5. an adjustment to the net amount in item 3 by six months of interest, accrued at the approved nominal rate of return; and
6. a summation of the above amounts to derive the closing balance for each year.

Evoenergy proposes to provide details of its calculations in the format set out in Table 11.3. In proposing variations to the amount and structure of Jurisdictional Scheme charges, Evoenergy's target is to achieve a zero expected balance on its Jurisdictional Scheme overs and unders account at the end of each regulatory year in the next regulatory control period. If this closing balance is not zero at the completion of each regulatory year, the difference between zero and the final amount will be taken into account when setting prices for the following year.

Table 11.3 Indicative calculation of Evoenergy’s Jurisdictional Scheme overs and unders account

\$'000	2015/16 Actual	2016/17 Estimate	2017/18 Forecast
Jurisdictional Scheme revenue			
Total Jurisdictional Scheme related revenue	28,639	29,363	69,751
Feed-in Tariffs (small & medium scale)	14,359	16,045	16,580
Feed-in Tariffs (large scale)	6,036	6,235	19,930
Administration	0	120	123
Utilities Network Facilities Tax	6,478	7,111	7,609
Energy Industry Levy	1,058	768	1,276
Total Jurisdictional Scheme related payments	27,931	30,279	45,517
Over (under) recovery for the financial year	708	-917	24,234
Overs and unders account			
Annual rate of interest applicable to balances	6.38%	6.35%	6.30%
Semi-annual interest rate	3.14%	3.13%	3.10%
Opening balance	2,835	3,747	3,039
Interest on opening balance	181	238	191
Over/under recovery for financial year	708	-917	24,234
Interest on over/under recovery	22	-29	751
Closing balance	3,747	3,039	28,215

While the method of reporting Jurisdictional Scheme revenue is proposed to remain unchanged, the process to derive the forecast amount of revenue to be recovered through jurisdictional schemes will change. For years up to and including 2017–18, Evoenergy forecast the amount of revenue to recover in jurisdictional schemes, and reflected this in its network pricing. From 2018–19 onwards, this process will change in

line with the passing of the *Electricity Feed-in (Large Scale Renewable Energy Generation) Amendment Act 2017* (ACT) through the ACT Legislative Assembly in September 2017.⁷ The insertion of some additional steps in the process will provide greater clarity to the ACT Government, for whom the Jurisdictional Scheme amounts are calculated.

The Electricity Feed-in Amendment Act 2017 outlined new requirements Evoenergy must follow in regards to jurisdictional schemes. Under the Act, Evoenergy is required to provide the ACT Government with estimates of (a) Feed-in Tariff support payments; and (b) costs to administer Feed-in Tariff support payments, no later than 31 December each year. Both costs are to be provided for the 'financial year preceding the current financial year' and the 'upcoming financial year and the following 4 financial years' (i.e. six years in total). If the application (i.e. lodgement of costs) does not contain sufficient information, the Minister may require further information within 10 business days of the request. The Minister must make a 'reasonable costs determination for the upcoming financial year no later than 2 months' (i.e. by end February) after Evoenergy provides the costs to the Minister. Evoenergy will subsequently determine Jurisdictional Scheme pricing based on the approved revenue amounts.

⁷ Source: http://www.legislation.act.gov.au/b/db_56843/current/pdf/db_56843.pdf.

Shortened forms

Term	Meaning
ABS	Australian Bureau of Statistics
ACT	Australian Capital Territory
AER	Australian Energy Regulator
CPI	Consumer Price Index
DNSP	Distribution Network Service Provider
DUOS	Distribution Use of System
PTRM	post tax revenue model
Rules	National Electricity Rules
SCS	Standard Control Services
STPIS	Service Target Performance Incentive Scheme
TUOS	Transmission Use of System