



Jemena Electricity Networks (Vic) Ltd

2021-26 Electricity Distribution Price Review Revised Proposal

Attachment 07-01

Response to the AER's draft decision - Price control mechanisms



Table of contents

Glossary	iii
Abbreviations	iv
Overview	v
1. Introduction	1
1.1 Price control mechanism – direct control services.....	1
2. Standard control services	2
3. Type 5 and 6 (smart metering) services	6
4. Alternative control services	9
4.1 Fee based services	9
4.2 Quoted services.....	9
5. Designated pricing proposal charges	12
6. Jurisdictional cost recovery scheme	13
7. Annual pricing proposal revenue true-ups	14

Glossary

current regulatory period	The regulatory control period covering 1 January 2016 to 31 December 2020
draft decision	The draft decision on the determination that will apply to setting JEN's distribution prices for the next regulatory period
F&A paper	Framework and approach paper ¹
initial proposal	The initial regulatory proposal to the AER for the setting of regulated pricing for JEN for the next regulatory period
intervening period	The period covering 1 January 2021 to 30 June 2021 representing the time between the end of the current regulatory period and the commencement of the next regulatory period.
next regulatory period	The regulatory control period covering 1 July 2021 to 30 June 2026
market participant fees	Fees charged by AEMO to market participants in accordance with their electricity fee structure determination.
revised proposal	The revised regulatory proposal to the AER for the setting of regulated pricing for JEN for the next regulatory period, of which this document forms part.

¹ AER, *Final framework and approach, Victorian distributors, Regulatory control period commencing 1 January 2021*, January 2019. Note, since the release of the F&A paper the date for commencement of the next regulatory period has been shifted to 1 July 2021.

Abbreviations

ABS	Australian Bureau of Statistics
ACS	Alternative Control Services
AMI-OIC	Advanced Metering Infrastructure Order in Council
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
CPI	Consumer Price Index
DUoS	Distribution Use of System
DMIA	Demand Management Incentive Allowance
DMIAM	Demand Management Incentive Allowance Mechanism
DMIS	Demand Management Incentive Scheme
DNSP	Distribution Network Service Provider
DPPC	Designated Pricing Proposal Charges
ESC	Essential Services Commission of Victoria
FRC	Full Retail Contestability
JEN	Jemena Electricity Network
JCRS	Jurisdictional Costs Recovery Scheme
MSATS	Metering Settlement and Transfer System
NEM	National Electricity Market
NER	National Electricity Rules
PTRM	Post Tax Revenue Model
SCS	Standard Control Services
STPIS	Service Target Performance Incentive Scheme
TNSP	Transmission Network Service Provider
WACC	Weighted Average Cost of Capital

Overview

This Attachment outlines how we propose to adjust our prices for direct control services for each year of the 2021-26 regulatory control period (**next regulatory period**). It also outlines how we will comply with the requirements of the National Electricity Rules (**NER**)² that relate to setting prices.

In late September, the Australian Energy Regulator (**AER**) issued its draft decision (**draft decision**) outlining its approach to setting allowable revenues and prices for the next regulatory period. As a part of this decision, the AER outlined how it would control prices and revenues. The draft decision largely adopts the previous practices for setting revenues in the current regulatory period and are outlined in the final framework and approach paper (**F&A paper**), updated via AER subsequent notifications³. We agree with the majority of positions taken in the AER's draft decision. However, we seek two changes as part of this revised proposal; these are:

- expanding the items within the B factor term to account for market participant fees that potentially could be charged to Jemena Electricity Networks (**JEN**) by the Australian Energy Market Operator (**AEMO**) during the next regulatory period
- the inclusion of margin for quoted services, given the identical circumstances that led to this allowance being approved for other Distribution Network Service Providers (**DNSPs**).

We note that the F&A paper is binding on the price reset process, and deviations can only be adopted if there is a material change in circumstance. Concerning the two issues noted above, we believe the items are material in nature, with the potential⁴ for AEMO fees not being identified until August 2020 and the timing of the events surrounding margin falling so close to the F&A as to prevent its inclusion.

Customer impact

What price control mechanisms mean for our customers?

Price control formulae benefit our customers in three key ways:

- When speaking to our customers, they told us affordability was important to them.⁵ The price control mechanisms give assurance that the prices implemented will not to breach the predetermined revenue allowances. This gives our customers comfort regarding the prices they pay for distribution services and this goes some way towards addressing their affordability concerns.
- Our customers have told us that they value consistency and certainty in their bills.⁶ They told us they manage budgets and that they could do this better if they knew what was coming up.

Whilst most of the bill impacts are driven by the revenue determination price path, the revenue and price control formula also contributes to the stability in prices and bills from year to year. Having these formulae prescribed at the commencement of the next regulatory period gives our customers confidence and certainty around the process for setting prices and that there is a degree of stability in pricing.

- The side constraints in the standard control services revenue and smart metering service revenues also provide a further layer of certainty to ensure price stability.

² NER, clause 6.2.5.

³ Emails from the AER to JemenaEDPR2021@jemena.com.au, 2 December 2019, 5:16pm and from AER to Jemena staff on 19 December 2019, 11:45am and on 15 January 2020 at 5:06pm.

⁴ This potential becomes likely with the release of AEMO's draft decision which seeks to charge DNSPs participant fees. AEMO, *Electricity Fee Structures, Draft Report and Determination*, November, 2020.

⁵ JEN, *2021-26 Electricity Distribution Price Review, Regulatory Proposal, Attachment 02-02, Community engagement report*, p. 43.

⁶ JEN, *2021-26 Electricity Distribution Price Review, Regulatory Proposal, Attachment 02-04, Reconvening the Jemena People's panel*, 31 January 2020, Section 3.1

JEN's response in this revised proposal

Other than these adjustments, we have adopted (i) the control mechanisms and (ii) the unders and overs account approaches to setting prices as set out in the AER's draft decision. A summary of the key draft decision items and our response to each is outlined in Table OV-1.

Table OV-1: Description of AER's draft decision and JEN response

Key draft decision description	AER positions	JEN response
The form of control mechanism for standard control services (SCS)	Revenue cap	Accept
The form of control mechanism for type 5 and 6 (including smart metering) services, classified as an alternative control service (ACS)	Revenue cap	Accept
The form of control mechanism for all other alternative control service ⁷	Price cap	Accept
Revenue cap formula for standard control services	The formula set out in Figure 14.1 of Attachment 14 of the draft decision, with side constraints set out in Figure 14.2	Partially accept – We propose that the AER includes the recovery of market participant fees within the B factor term. JEN's liability for these fees is a foreseeable regulatory requirement from AEMO's current consultation, which JEN has no control over.
Revenue cap formula for type 5 and 6 (including smart metering) services	The formula set out in Figure 14.3 of Attachment 14 of the draft decision, with the price cap formula for quoted services set out in Figure 14.6	Accept
Price cap formula for all other alternative control service	Price cap formula for prices set in advance as set out in Figure 14.5 of Attachment 14 of the draft decision, with side constraints set out in Figure 14.4	Partially accept – We propose that the AER includes the margin for quoted services as there are no differing circumstances to how this was allowed for other distribution networks
Distribution Use of System (DUoS) unders and overs account method	Method set out in Appendix A Attachment 14 of the draft decision	Accept
Type 5 & 6 (including smart meter) services unders and overs account method	Method set out in Appendix B Attachment 14 of the draft decision	Accept
Designated pricing proposal charges unders and overs account method	Method set out in Appendix C Attachment 14 of the draft decision	Accept
Jurisdictional scheme amounts unders and overs account method	Method set out in Appendix D Attachment 14 of the draft decision	Accept
Rounding of inputs in annual pricing proposals	Method set out in Appendix E Attachment 14 of the draft decision	Accept

⁷ These include network ancillary services, auxiliary and type 7 metering services, basic and enhanced connection services, connection application and management services and public lighting services.

1. Introduction

This attachment of our revised proposal outlines our response to the AER's draft decision on the mechanisms under which it controls the way prices are set for JEN's direct control services. It also raises additional material changes in circumstances concerning price controls that have arisen since submitting our initial proposal.

By adhering to the formulae outlined in this attachment, JEN considers it would meet the requirement of clause 6.12.1(13) of the NER, to demonstrate compliance with the relevant control mechanism.

1.1 Price control mechanism – direct control services

The AER's draft decision sets out the price control mechanism that JEN applies to determine charges applicable for the direct control services offered in the next regulatory period. These charges are adjusted annually via an annual pricing proposal. We will submit an initial pricing proposal following the AER's final determination on this regulatory proposal and then submit an annual pricing proposal by 31 March of each remaining year in the next regulatory period.⁸

The price control mechanisms for direct control services include:

- A revenue cap for standard control services (refer Box 2-1), with side constraint (refer Box 2-2)
- A revenue cap for type 5, type 6 and smart metering services (refer to Box 3-1), with side constraint (refer Box 3-2)
- Caps on the prices for other services classified as alternative control service (refer to Box 4-1 and Box 4-2).

We also outline the approach to true-up revenue recovery from one year to the next for standard control services, type 5, type 6 and smart metering services, designated pricing proposal charges (**DPPC**) and jurisdictional cost recovery scheme (**JCRS**) charges (refer to Box 7-1).

⁸ Should 31 March fall on a weekend or public holiday then the submission will be by the first business day following 31 March.

2. Standard control services

Since lodging our initial proposal, AEMO has made a Draft Determination⁹ on its future electricity fee structures that will apply from 1 July 2021. It is seeking stakeholder views on the draft report and determination. The Final Determination and report is required to be published by 31 March 2021.

In the in Draft Determination, AEMO proposes to maintain the existing allocation of core NEM fees to Generators and Market Customers for the first two years of the next fee period (that is the transition period); and then introduce a separate allocation of the core NEM function costs to Transmission Network Service Provider's (TNSP) and to DNSPs from 1 July 2023. The fees to reflect the extent of TNSP and DNSP involvement with AEMO's core NEM activities, on the basis of energy consumed.¹⁰

JEN understands that the potential market participant fees for DNSPs relates to the standard control services.

Should AEMO commence charging these fees to DNSPs, JEN would be materially impacted, with additional costs being incurred. The costs are:

- the result of regulatory requirements, which are akin to Essential Services Commission (ESC) licence fees
- not included in our operating expenditure base year amount or any other opex component given we have not historically paid AEMO fees
- not yet known, so no conclusion can be reached as to how they might otherwise be recovered (for example, through the rate of change)
- not controllable – that is, JEN cannot influence the magnitude of the expense.

This revenue cap control mechanism formula includes a cost recovery mechanism as set out in our final F&A paper. The F&A paper provides for the annual adjustment factors to be included in the B-factor to be decided in the distribution determination. In the draft decision, the AER has allowed the Victorian DNSPs to continue recovery of the ESC fees via the B factor.

We consider AEMO's Draft Determination to levy fees on DNSPs is a material change in circumstances since the F&A¹¹ was published and the NER provides the AER to depart from the control mechanism formulae in F&A.¹² We propose the AEMO fee be also be included in the B factor in the distribution determination.

We consider that it is appropriate that these fees should be treated as an automatic cost recovery from customers via the price control mechanisms, in the same way that ESC licence fees currently are. For the avoidance of doubt, if the AEMO proposal is ultimately not implemented or these fees are not incurred by JEN, there would be no associated cost recovery.

We note that a regulated network service provider should be afforded a reasonable opportunity to recover at least its efficient costs.¹³ We consider that the approach outlined in this section of the revised proposal is the most appropriate mechanism to recover these expenses, given the uncontrolled nature of these costs. Should the AER consider the mechanism proposed not to be right, we propose the costs—potentially and necessarily incurred—are efficient, and therefore, an alternative mechanism should be identified. That is, the costs themselves cannot be rejected on the basis of a different mechanism to recover the costs; the AER should consider the efficiency of the cost first, then the appropriate mechanism for recovery.

This is a new issue for inclusion in the AER's final decision and has been included in the B factor terms of our revised revenue cap formula in Box 2-1 and Box 3-1. Other than the revised B factor terms, all elements of the

⁹ AEMO, *Electricity Fee Structures, Draft Report and Determination*, November 2020.

¹⁰ *Ibid.*, p. 5.

¹¹ AER, *Final framework and approach, Victorian distributors, Regulatory control period commencing 1 January 2021*, January 2019. Note, since the release of the F&A paper the date for commencement of the next regulatory period has been shifted to 1 July 2021

¹² NER, cl 6.12.3(c1).

¹³ National Electricity Law, s7A(2).

revenue cap formula are consistent with the approach outlined in the AER's draft decision. The method for trueing up revenues under the standard control services revenue cap is outlined in section 7 of this document.

Box 2-1. Revenue cap formula for standard control services

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

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

$$(3) \quad AAR_t = AR_t \quad t = 1$$

$$(4) \quad AAR_t = AAR_{t-1} \times (1 + \Delta CPI_t) \times (1 - X_t) \quad t = 2, 3,\dots, 5$$

Where:

TAR_t is the maximum 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 .

I_t is the sum of incentive scheme adjustments in year t . Likely to incorporate revenue adjustments relating to outcomes of:

- the fire start incentive scheme (f-factor) in relation to financial year $t-3$ to be applied in years $t=1$ to 5 (e.g. 2018/19 f-factor to be applied in 2021-22)
- the STPIS in relation to:
 - regulatory year $t-3$ to be applied in years $t=1,2$ (i.e. 2019 STPIS to be applied in 2021-22, 2020 STPIS to be applied in 2022-23)
 - regulatory year $t-2$ to be applied in years $t=2$ to 5 (i.e. 2021 6-month STPIS to be applied in 2022-23, 2021-22 STPIS to be applied in 2023-24, and so on).¹⁴
- the demand management incentive scheme (**DMIS**) in relation to:
 - regulatory year $t-3$ to be applied in years $t=1,2$ (i.e. 2019 DMIS to be applied in 2021-22, 2020 DMIS to be applied in 2022-23)
 - regulatory year $t-2$ to be applied in years $t=2$ to 5 (i.e. 6-month DMIS to be applied in 2022-23, 2021-22 DMIS to be applied in 2023-24, and so on).¹⁵
- the demand management innovation allowance (**DMIA**) in relation to the 2016-20 regulatory period¹⁶ to be applied in regulatory year $t=2$ only¹⁷
- any other related incentive schemes as applicable that are to be applied in year t .

B_t is the sum of annual adjustment factors for year t . It includes:

- the true-up for any under or over recovery of actual revenue collected through DUoS charges calculated using the following method:

¹⁴ In the year 2022-23, the STPIS performance outcomes for both the 2020 year and the 2021 6-month period will be applied.

¹⁵ In the year 2022-23, the DMIS performance outcomes for both the 2020 year and the 2021 6-month period will be applied.

¹⁶ The DMIA measurement will be extended to incorporate the 2021 six month period.

¹⁷ The DMIA will be replaced by the demand management innovation allowance mechanism (**DMIAM**) from 1 June 2021 and will be applied in year 2 of the 2026-31 regulatory control period.

$$DUoS \text{ Under and Overs True} - Up_t = - (Opening \text{ Balance}_t) (1 + WACC_t)^{0.5}$$

Where:

DUoS Under and Overs True – Up_t is the true-up for the balance of the DUoS unders and overs account in year t.

Opening Balance_t is the opening balance of the DUoS unders and overs account in year t as calculated by the method in Appendix A of Attachment 14 of the AER draft decision.

WACC_t is the approved weighted average cost of capital (**WACC**) used in regulatory year t in the DUoS unders and overs account in Appendix A of Attachment 14 of the AER draft decision. This WACC figure will be a nominal WACC figure that reflects actual inflation rather than forecast inflation. To calculate this nominal WACC, the real vanilla WACC from the annual update PTRM will be escalated for actual inflation.

- License fee charges incurred by the distributor, charged by the Victorian Essential Services Commission. The recovery of license fee charges will occur on a two-year lag, and will therefore be indexed by two years interest, calculated using the following method:

$$L_{t-2} \times (1 + WACC_t) \times (1 + WACC_{t-1})$$

- Market participant fee charges incurred by the distributor, charged by the Australian Energy Market Operator. The recovery of market participant fee charges will occur on a two-year lag, and will therefore be indexed by two years interest, calculated using the following method:

$$M_{t-2} \times (1 + WACC_t) \times (1 + WACC_{t-1})$$

Where:

L_{t-2} is the sum of the license fees paid by the distributor to the Victorian Essential Services Commission relating to regulatory year t-2. As these license fees are calculated on a financial year, there is no consideration required for transitioning this factor across the move to financial years.

M_{t-2} is the sum of the market participant fees paid by the distributor to the Australian Energy Market Operator relating to regulatory year t-2.

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 regulatory year t.

ΔCPI_t is the annual percentage change in the ABS consumer price index (**CPI**) All Groups, Weighted Average of Eight Capital Cities 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 2021-22, year t-2 is the December quarter 2019 and year t-1 is the December quarter 2020.

X_t is the X-factor for each year of the 2021-26 regulatory control period as determined in the PTRM, and annually revised for the return on debt update in accordance with the formula specified in attachment 3-rate of return- calculated for the relevant year.

Box 2-2 contains the side constraint formula for standard control services, consistent with the draft decision.

Box 2-2. Side constraint formula

For $t=2,3,\dots,5$:

$$\frac{(\sum_{i=1}^n \sum_{j=1}^m p_t^{ij} q_t^{ij})}{(\sum_{i=1}^n \sum_{j=1}^m p_{t-1}^{ij} q_t^{ij})} \leq (1 + \Delta CPI_t) \times (1 - X_t) \times (1 + 2\%) + I'_t + B'_t + C'_t$$

Where each tariff class has “n” tariffs, with each up to “m” components, and where:

p_t^{ij} is the proposed price of component ‘j’ of tariff ‘i’ for year t.

p_{t-1}^{ij} Is the price charged for component ‘j’ of tariff ‘i’ in year t-1.

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

ΔCPI_t is the annual percentage change in the ABS CPI All Groups, Weighted Average of Eight Capital Cities 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 2021-22, year t-2 is the December quarter 2019 and year t-1 is the December quarter 2020.

X_t is the X-factor for each year of the 2021-26 regulatory control period as determined in the PTRM, and annually revised for the return on debt update in accordance with the formula specified in attachment 3-rate of return-calculated for the relevant year. If $X > 0$, the X will be set equal to zero for the purposes of the side constraint formula.

I'_t is the annual percentage change in the sum of incentive scheme adjustments described in Box 1-1 applied in year t. This percentage should be calculated by dividing the incremental revenues (the difference between the I-factor used in the total annual revenue formula for t and t-1) by the expected revenues for regulatory year t-1 (based on prices in year t-1 multiplied by the forecast quantities for year t).

B'_t is the annual percentage change from the sum of annual adjustment factors for year t and includes true-up for any under or over recovery of actual revenue collected through DUoS charges calculated using the method in Box 1-1. This percentage should be calculated by dividing the incremental revenues (as used in the total annual revenue formula) for each factor by the expected revenues for regulatory year t-1 (based on prices in year t-1 multiplied by the forecast quantities for year t).

C'_t is the annual percentage change from 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 adjustment in regulatory year t. This percentage should be calculated by dividing the incremental revenues (the difference between the C-factor used in the total annual revenue formula for t and t-1 multiplied by the forecast quantities for year t).

3. Type 5 and 6 (smart metering) services

Box 3-1 contains our proposed revenue cap formula for type 5 and 6 services. Other than the revision to the B factor term for reasons noted above, it is consistent with the approach outlined in the draft decision. The method for trueing up revenues under the revenue cap for of regulation is outlined in section 7.

Similar to the approach for recovering AEMO market participant fees under standard control services, we also seek to recover market participant fees for metering functions performed by JEN in it's capacity as meter data provider, meter provider, metering coordinator.

At the time of publishing it's draft determination on allocating market participant fees, AEMO indicated it would not charge market participant fees to other market participant types. However, as AEMO's publication is still in draft the final determination could change, meaning we may be charged for market participant fees in our metering related services. Given this, and with the clear material change in circumstances since issuing the F&A paper, we consider adding the ability to recover market participant fees in the smart metering services price control formula is the most appropriate mechanism to ensure we are afforded a reasonable opportunity to recover our efficient costs.

Box 3-1. Revenue cap formula (type 5 and 6 (inc. smart metering) services)

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

$$(2) TARM_t = AR_t + T_t + B_t + C_t \quad t=1, 2, \dots, 5$$

$$(3) AR_t = AR_{t-1}(1 + \Delta CPI_t) \times (1 - X_t) \quad t=2, 3, 4, 5$$

Where:

$TARM_t$ is the total allowable revenue for type 5 and 6 (inc. smart metering) services 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 for year t. In year t=1, the annual smoothed revenue requirement is set in the final decision PTRM.

AR_{t-1} this is annual smoothed revenue requirement approved for year t-1.

T_t Is the adjustments in year t for true-ups relating to the AMI-OIC. There are no adjustments expected for the 2021-26 regulatory control period, and therefore the T factor will have a value of 0.

B_t is the sum of annual adjustment factors for year t. It includes:

- the true-up for any under or over recovery of actual revenue collected through type 5 and 6 (inc. smart metering) charges calculated using the following method:

$$\text{Metering Under and Overs True} - Up_t = - (\text{Opening Balance}_t) (1 + WACC_t)^{0.5}$$

Where:

Metering Unders and Overs True – Up_t is the true-up for the balance of the type 5 and 6 (inc. smart metering) services unders and overs account in year t.

Opening Balance_t is the opening balance of the type 5 and 6 (inc. smart metering) services unders and overs account in year t as calculated by the method in appendix B of Attachment 14 of the AER draft decision.

WACC_t is the approved weighted average cost of capital used in regulatory year t in the type 5 and 6 (inc. smart metering) services unders and overs account in appendix B Attachment 14 of the AER draft decision. This WACC figure will be a nominal WACC figure that reflects actual inflation rather than forecast inflation. To calculate this nominal WACC, the real vanilla WACC from the annual update type 5 and 6 (inc. smart metering) services PTRM will be escalated for actual inflation.

- Market participant fee charges incurred by the distributor in its capacity as a metering coordinator, charged by the Australian Energy Market Operator. The recovery of market participant fee charges will occur on a two-year lag, and will therefore be indexed by two years interest, calculated using the following method:

$$M_{t-2} \times (1 + WACC_t) \times (1 + WACC_{t-1})$$

Where:

M_{t-2} is the sum of the market participant fees paid by the distributor to the Australian Energy Market Operator relating to regulatory year t-2.

C_t is the sum of approved cost pass-through amounts (positive or negative) attributed to these metering services with respect to regulatory year t, as determined by the AER. It will also include any applicable end-of-period adjustments in regulatory year t.

ΔCPI_t is the annual percentage change in the ABS CPI All Groups, Weighted Average of Eight Capital Cities from 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 2021-22, year t-2 is the December quarter 2019 and year t-1 is the December quarter 2020.

X_t is the X-factor for each year of the 2021-26 regulatory control period as determined in the metering PTRM, and annually revised for the return on debt update in accordance with the formula specified in attachment 3 of the AER draft decision, calculated for the relevant year. This annual update of the metering PTRM will be provided alongside (or prior to) the pre-populated pricing model template prior to submission of the annual pricing proposal each year.

Box 3-2 contains the side constraint formula for Type 5 and 6 (smart metering) services, consistent with the draft decision.

Box 3-2. Side constraints formula

For $t=2, 3, 4, 5$:

$$\frac{p_t^i}{p_{t-1}^i} \leq (1 + \Delta CPI_t) \times (1 - X_t) \times (1 + 2\%) + T_t' + B_t' + C_t'$$

Where:

p_t^{ij} is the proposed price for tariff 'i' for year t.

p_{t-1}^{ij} is the price charged for tariff 'i' in year t-1.

ΔCPI_t is the annual percentage change in the ABS CPI All Groups, Weighted Average of Eight Capital Cities 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 2021-22, year t-2 is the December quarter 2019 and year t-1 is the December quarter 2020.

X_t is the X-factor for each year of the 2021-26 regulatory control period as determined in the metering PTRM, and annually revised for the return on debt update in accordance with the formula specified in attachment 3-rate of return-calculated for the relevant year. This annual update of the metering PTRM will be provided alongside (or prior to) the pre-populated pricing model template prior to submission of the annual pricing proposal each year.

T_t is the annual percentage change from the sum of annual adjustment factors for year t relating to the AMI-OIC. There are no adjustments expected for the 2021-26 regulatory control period, and therefore the T-factor will have a value of 0.

B_t' is the annual percentage change from the sum of annual adjustment factors for year t and includes true-up for any under or over recovery of actual revenue collected through type 5 and 6 (inc. smart metering) services charges calculated using the method in Figure 14.3.

C_t' is the annual percentage change from the sum of approved cost pass through amounts (positive or negative) attributed to these metering services with respect to regulatory year t, as determined by the AER. It will also include any applicable end-of-period adjustment in regulatory year t. This percentage should be calculated by dividing the incremental revenues (the difference between the C-factor used in the total annual revenue formula for t and t-1 multiplied by the forecast quantities for year t).

With the exception of the CPI and X-factor, the percentage for each of the other factors above can be calculated by dividing the incremental revenues (as used in the total annual revenue formula) for each factor by the expected revenues for regulatory year t-1 (based on the prices in year t-1 multiplied by the forecast quantities for year t).

4. Alternative control services

4.1 Fee based services

Box 4-1 contains the price cap formula for the fee based alternative control service . This replicates the draft decision.

Box 4-1. Price cap formula to apply to JEN's fee-based alternative control services

$$\bar{p}_t^i \geq p_t^i \quad i=1,\dots,n \text{ and } t=1,2,\dots,5$$

$$\bar{p}_t^i = \bar{p}_{t-1}^i \times (1 + \Delta CPI_t) \times (1 - X_t^i) + A_t^i$$

Where:

\bar{p}_t^i is the cap on the price of service i in year t.

p_t^i is the price of service i in year t. For the first year of the regulatory control period, the cap on the price of service i will be as per the schedule of approved charges set out in the AER final decision.

\bar{p}_{t-1}^i is the cap on the price of service i in year t-1.

t is the regulatory year.

ΔCPI_t is the annual percentage change in the ABS CPI All Groups, Weighted Average of Eight Capital Cities 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 2021-22, year t-2 is the December quarter 2019 and year t-1 is the December quarter 2020.

X_t^i is the X-factor for service i in year t. The value of this factor is as specified in the AER final decision.

A_t^i is the sum of any adjustments for service i in year t. Likely to include, but not limited to adjustments for any approved cost pass-through amounts (positive or negative) with respect to regulatory year t, as determined by the AER.

4.2 Quoted services

In our initial proposal, JEN proposed labour rates for use in the price cap formula for services charged on a quotation basis. Further, we proposed the addition of tax and margin components to the pricing formula for alternative control service charged on a quotation basis.

In our revised proposal, we accept the AER's rejection of tax being added to the price cap formula for services charged on a quotation basis.

However, we believe our initial proposal position to add a margin to the pricing formula is consistent with the AER's determinations for TasNetworks and SA Power Networks and the approach supported by the AER's consultant, Marsden Jacob, for the NSW, ACT, NT and TAS proposals, where the consultant accepted the inclusion of a profit margin.¹⁸

¹⁸ Marsden Jacob, *Marsden Jacob Report prepared for AER, Review of Alternative Control Services*, September 2018, p. 7.

We note that at the time the SA Power Networks responded to the preliminary Framework and Approach (April 2018), the AER had not made the draft decision for TasNetworks (September 2018). However, in the draft decision for SA Power Networks, the AER notes:

This means that, at the time of the F&A, our determination for TasNetworks to include a margin as an explicit additional factor within the control mechanism formula had not been made. We consider that this material change in circumstances warrants a different approach to that set out in our final F&A for SA Power Networks.¹⁹

We understand that the basis for rejecting JEN's proposal for a margin on quoted services—and the reason for the difference to the SA Power Networks decision—is that the decision for TasNetworks decision was *not* known at the time of when SA Power Networks was preparing its submission. However, the AER's draft decision for JEN implies that the TasNetworks decision was known at the time of JEN responding to the F&A consultation (November 2020) and therefore should have proposed the addition of a margin component to the price cap formula at the preliminary F&A stage. In all other respects, the circumstances faced by JEN and all other DNSPs are identical. These include:

- NER requirements
- NER timing obligations
- decisions made
- the materiality of the issues – notably, we proposed a WACC as the basis for the margin, consistent with the approach adopted in SA Power Networks final decision; we consider the materiality threshold to be the same for JEN.

We do not consider the timing of the submission and decisions of other network businesses has a bearing on the decision to reject JEN's application for marking a proposal to include a margin in the price control for quoted services. Instead, we consider the substance should be preferred over form and that the merits of the situation should take primacy over an administrative timing issue.

Contestable works

DNSPs in Victoria are required to provide contestability of connection and augmentation works in accordance with the Essential Services Commission's Guideline 14.²⁰ We are required to publish tendering policies that inform customers' contestability rights and options in regard to connection to JEN's shared network. JEN's contestable works guideline²¹ and connection policy reflect the objectives of Guideline 14. JEN's connection policy allows competition of design and construction of connection assets, network extensions and real estate developments.²² Other competitive services connection and connection management services, undergrounding of overhead supplies, temporary connections (> 100 amps), design and construction of new public lighting.

We consider including an explicit margin within the price cap formula for quoted services:

- reflects the principle of competitive neutrality
- would assist in promoting the development of competition
- would assist in achieving consistency between regulatory arrangements for similar services across all jurisdictions.²³

Box 4-2 contains JEN's proposed price control formula for quoted services.

¹⁹ AER, Draft decision, SA Power Networks Distribution Determination 2020 to 2025, Attachment 13 Control mechanisms, October 2019, p. 17.

²⁰ Essential Services Commission, *Electricity Industry Guideline No. 14*, April 2004, section 4.

²¹ JEN, *Contestable Works Guideline*, 26 November 2019.

²² JEN, *Connection Policy*, 30 June 2016, section 3.7.3.

²³ NER, cl 6.2.5(d)(4).

Box 4-2. Price cap formula to apply to JEN's quoted alternative control services

$$Price = Labour + Contractor Services + Materials + Margin$$

Where:

Labour consists of all labour costs directly incurred in the provision of the service, which may include labour on-costs, fleet on-costs and overheads. Labour is escalated annually by $(1+\Delta CPI_t)(1-X_t^i)$ where:

ΔCPI_t is the annual percentage change in the ABS CPI All Groups, Weighted Average of Eight Capital Cities²⁴ 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 2021-22, year t-2 is the December quarter 2019 and year t-1 is the December quarter 2020.

X_t^i is the X factor for service i in year t, The value of this factor is as specified in the AER final decision.

Contractor services reflects all costs associated with the use of external labour including overheads and any direct costs incurred. The contracted services charge applies the rates under existing contractual arrangements. Direct costs incurred are passed on to the customer.

Materials reflects the cost of materials directly incurred in the provision of the service, material storage and logistics on-costs and overheads.

Margin is an amount equal to JEN's nominal vanilla WACC applied to the total cost of Labour, Contractor Services and Materials

²⁴ If the ABS do not, or ceases to, publish the index, then CPI will mean an index which the AER considers is the best available alternative index.

5. Designated pricing proposal charges

DPPC²⁵ recover the payments we make for:

- Transmission charges, which are payments for using a TNSP high voltage network
- Inter-DNSP charges which relate to cross-boundary settlements between networks. This applies when an adjoining distribution network supplies customers located near JEN's network border
- Amounts paid for avoided transmission services in accordance with clause 5.5(j) of the NER. There are payments recognising that energy supplied to the DNSP by an embedded generator (e.g. large scale solar and wind farms) would have otherwise been supplied from a TNSP's high voltage network.

To recover these charges, JEN will include the true-up method as required by the draft decision for the under or over recovery of DPPC costs incurred during the t-2 year. The method adjusts for the time value of money by calculating the present value of actual DPPC revenue equal to the present value of recoverable charges. The mechanism to recover these charges is described in Appendix C of Attachment 14 of the AER's draft decision and is outlined in section 7 of this document.

²⁵ NER cl. 6.18.7.

6. Jurisdictional cost recovery scheme

JCRS provides for cost recovery for services that are required within the Victorian jurisdiction. These include, but not limited to, rebates for the Premium Feed-in tariff.

JEN will include a true-up as required by the draft decision and NER for the under or over recovery of JCRS costs incurred during the t-2 year as part of its annual pricing proposal. The method adjusts for the time value of money by calculating the present value of actual JCRS revenue equal to the present value of recoverable charges. The mechanism to achieve this is described in Appendix D of Attachment 14 of the AER's draft decision and is outlined in section 7 of this document.

7. Annual pricing proposal revenue true-ups

The revenue cap form of price control requires a true-up of the actual revenue received as it varies to revenue allowance—in the case of standard control services and type 5 and 6 regulated metering services—or costs—in the case of DPPC and JCRS.

To undertake these adjustments, we will follow the process demonstrated in Box 7-1.

In all calculations, the balance amounts must be adjusted for the time value of money using the WACC consistent with the rate approved by the AER in the final determination in the year in which the determination is applicable, i.e. the WACC in previous regulatory periods—updated for the trailing cost of debt—will be used where the formula crosses multiple regulatory periods.

Box 7-1 Demonstration of revenue true-up

In year t we are trueing up revenue under and over recoveries for t-2, and the over or under recovery in year t itself won't be trueed up until t+2. The following example demonstrates how we will perform the calculations:

	t-2	t-1	t
(A) Revenue from tariffs	247,500	247,000	249,511
(B) Allowed revenue	247,000	248,000	249,000
(C) Pass through	-	2	14
(D) Revenue under / (over) recovery (A) – ((B) + (C))	500	- 1,002	497
(E) WACC	10.00%	10.00%	10.00%
(F) Opening balance (J) from t-1	-	524	- 474
(G) Interest on opening balance	-	52	- 47
(H) Revenue under / (over) recovery (D)	500	- 1,002	497
(I) Interest on under / (over) recovery ^[1]	24	- 49	24
(J) Closing balance (F) + (G) + (H) + (I)	524	- 474	0 ^[2]

[1] Calculated using a half year effect on the WACC, i.e., $(1+WACC)^{0.5-1}$

[2] Must set tariffs at rates that cause this value to be close to zero

The revenue true-ups will also cover the intervening period. Specifically, this will include:

- For t=1=2021-22, the unders/overs accounts (for standard control services, metering, DPPC, and JCRS) will incorporate four periods: 2019 actuals, 2020 estimates, 2021 intervening period estimates, and 2021-22 forecasts
- For t=2=2022-23, the unders/overs accounts (for standard control services, metering, DPPC, and JCRS) will incorporate four periods: 2020 actuals, 2021 intervening period actuals, 2021-22 estimates, and 2022-23 forecasts

- For $t=3,4,5$, the unders/overs accounts (for standard control services, metering, DPPC, and JCRS) will revert to the standard three periods: $t-2$ actuals, $t-1$ estimates, and t forecasts.