

30 January 2015

Mr Sebastian Roberts  
General Manager  
Australian Energy Regulator (AER)  
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By Email: [SAElectricity2015@accc.gov.au](mailto:SAElectricity2015@accc.gov.au); [AERInquiry@aer.gov.au](mailto:AERInquiry@aer.gov.au)

Dear Mr Roberts

## Proposed negotiated distribution service criteria – SA Power Networks

Thank you for the opportunity to make a submission on the AER's proposed negotiated distribution service criteria (NDSC)<sup>1</sup> for the regulatory control period commencing 1 July 2015.

We have two comments we would like to make on the proposed NDSC.

### NDSC numbering

SA Power Networks notes the proposed criteria are essentially the same as in the current NDSC, except the numbering has changed. The proposed NDSC lists the *National Electricity Objective*, three criteria under *Terms and Conditions of Access*, eight criteria under *Price of Services* and two criteria under *Access Charges*. These 13 items were previously numbered 1 through to 13 but in the current drafting the numbering has been restarted from 1 in each of these sections.

In undertaking this renumbering, the AER has inadvertently numbered a paragraph under *Price of Services* as criterion 4, whereas it should not be numbered - it is part of the previous criterion. Also, the references to criteria 7 and 8 appearing in *Price of Services* criterion 2 are now incorrect. We have corrected the criteria numbering and references in Attachment 1 to this letter.

### Costs of services

In South Australia there are many services classified as Negotiated Distribution Services that in other jurisdictions are classified as Alternative Control Services. In negotiating the prices of certain services with customers, it has been SA Power Networks' experience that negotiating parties can have differing interpretations of the meaning of the word 'costs'. That is, there is not a common understanding of the appropriate costs that a distributor may (or must) recover. This has been a contributing factor to protracted negotiations with some customers.

SA Power Networks' view is that negotiated distribution services charges should recover, at a minimum, the economic costs to provide the assets and services, including an allocation for overheads. These costs should include at least a return on the capital employed, using an appropriate weighted average cost of capital; the depreciation cost of the assets; the operating costs; and an allowance for tax obligations. These costs should be subject to indexation to account for inflation.

<sup>1</sup> AER, *Call for submissions – Proposed negotiated distribution service criteria for Energex, Ergon Energy and SA Power Networks – regulatory control period commencing 1 July 2015*, November 2014

However, in our experience, customers have disputed the legitimacy of some of these cost components and how they are treated, notwithstanding specific advice from relevant economic regulators and particularly the precedent provided by the Essential Services Commission of South Australia's determinations on this matter.

An example of the issues that such differences of interpretation can create is a current negotiation in respect of charges for a particular Negotiated Distribution Service. After approximately four years of information sharing and negotiation, SA Power Networks is currently participating in a formal dispute resolution process, the aim of which, at least as a first step, is to achieve a common understanding of the words 'costs incurred' in the NDSC. This seems a very meagre goal having already participated in several years of costly, unproductive and disruptive debate surrounding this issue.

SA Power Networks believes that more specifically defining the meaning of 'cost' in the NDSC could serve to reduce unnecessary costs for both sides of the negotiation. We assume our customers in the above example have incurred significant legal, accounting, consulting and administrative costs. For its part, SA Power Networks has incurred significant regulatory costs in developing agreements to facilitate negotiations (Memoranda of Understanding and Confidentiality Agreements), responding to information requests, providing independent accounting reports to verify information, providing pricing proposals, responding to counter-proposals, interstate travel, and obtaining legal advice. Also, the significant cost of the dispute resolution process itself will be shared.

To help clarify the costs that can be recovered and prevent future disputes of this nature arising, we would recommend that the AER amend the proposed NDSC to clarify that negotiated prices reflect the economic costs incurred by a distributor in providing these services.

In Attachment 1 we have proposed amendments in four places of the proposed NDSC to reflect this, for your consideration. We believe these changes would aid clarification that, for example, the return on capital and return of capital cost components are legitimate costs for inclusion in the pricing of negotiated services.

An alternative approach could be for "costs" to be explicitly defined as part of the NDSC. In our Proposed Negotiating Framework for 2015-20 which was Attachment 18.1 to our 2015-20 Regulatory Proposal, lodged with the AER on 31 October 2014, we proposed the following definition of costs:

*costs means any costs or expenses incurred by SA Power Networks in complying with this Negotiating Framework or otherwise advancing the Service Applicant's request for the provision of a negotiated distribution service and such other costs or expenses required to provide negotiated distribution services to a Service Applicant, consistent with the economic concepts applied to economic regulation under the Rules, and in compliance with SA Power Networks' Cost Allocation Methodology and any relevant part of a distribution determination applying to SA Power Networks.*

SA Power Networks trusts this submission will assist the AER in making its decision on the NDSC to apply from 1 July 2015. Please contact me or Wayne Lissner, Head of Regulation, on 08 8404 5391, if you would like to discuss these matters further.

Yours sincerely



Sean Kelly  
**General Manager Corporate Strategy**





## Attachment 1 - Proposed NDSC (amended by SA Power Networks)

1. The terms and conditions of access for a negotiated distribution service, including the price that is to be charged for the provision of that service and any access charges, should promote the achievement of the national electricity objective.

### Criteria for terms and conditions of access

#### *Terms and Conditions of Access*

2. The terms and conditions of access for a negotiated distribution service must be fair and reasonable and consistent with the safe and reliable operation of the power system in accordance with the NER.
3. The terms and conditions of access for a negotiated distribution service (including in particular, any exclusions and limitations of liability and indemnities) must not be unreasonably onerous taking into account the allocation of risk between a distributor and any other party, the price for the negotiated distribution service and the economic costs to a distributor of providing the negotiated distribution service.
4. The terms and conditions of access for a negotiated distribution service must take into account the need for the service to be provided in a manner that does not adversely affect the safe and reliable operation of the power system in accordance with the NER.

#### *Price of Services*

5. The price for a negotiated distribution service must reflect the economic costs that a distributor has incurred or incurs in providing that service, and must be determined in accordance with the principles and policies set out in the relevant Cost Allocation Method.
6. Subject to criteria 7 and 8, the price for a negotiated distribution service must be at least equal to the cost that would be avoided by not providing that service but no more than the cost of providing it on a stand-alone basis.
7. If a negotiated distribution service is a shared distribution service that:
  - i. exceeds any network performance requirements which it is required to meet under any relevant electricity legislation: or
  - ii. exceeds the network performance requirements set out in schedule 5.1a and 5.1 of the NER,



then the difference between the price for that service and the price for the shared distribution service which meets network performance requirements must reflect a distributor's incremental cost of providing that service (as appropriate).

8. If a negotiated distribution service is the provision of a shared distribution service that does not meet or exceed the network performance requirements, the difference between the price for that service and the price for the shared distribution service which meets, but does not exceed, the network performance requirements should reflect the cost a distributor would avoid by not providing that service (as appropriate).
9. The price for a negotiated distribution service must be the same for all Distribution Network Users unless there is a material difference in the costs of providing the negotiated distribution service to different Distribution Network Users or classes of Distribution Network Users.
10. The price for a negotiated distribution service must be subject to adjustment over time to the extent that the assets used to provide that service are subsequently used to provide services to another person, in which case such adjustment must reflect the extent to which the costs of that asset are being recovered through charges to that other person.
11. The price for a negotiated distribution service must be such as to enable a distributor to recover the efficient costs of complying with all regulatory obligations or requirements associated with the provision of the negotiated service.

### **Criteria for access charges**

#### ***Access Charges***

12. Any charges must be based on the economic costs reasonably incurred by a distributor in providing distribution network user access, and, in the case of compensation referred to in clauses 5.5(f)(4)(ii) and (iii) of the NER, on the revenue that is likely to be foregone and the costs that are likely to be incurred by a person referred to in those provisions where an event referred to in those provisions occurs (as appropriate).
13. Any charges must be based on the economic costs reasonably incurred by a distributor in providing transmission network user access to services deemed to be negotiated distribution services by clause 6.24.2(c) of the NER, and, in the case of compensation referred to in clauses 5.4A(h) to (j) of the NER, on the revenue that is likely to be foregone and the costs that are likely to be incurred by a person referred to in those provisions where an event referred to in those provisions occurs (as appropriate).

