Revised Proposed Pricing Methodology

2008/09 – 2013/14

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Contact

This document is the responsibility of the Regulatory & Business Strategy, SP AusNet.

Please contact the office below with any inquiries.

Eric Howie
Manager, Pricing
SP AusNet
Level 31, 2 Southbank Boulevard
Melbourne Victoria 3006
Ph: (03) 9695 6000

1. Introduction

Clause 6A.10.1 of the National Electricity Rules (NER) requires SP AusNet to submit a proposed pricing methodology to the Australian Energy Regulator (AER) at the same time that SP AusNet submits its revenue proposal.

SP AusNet submitted its proposed pricing methodology alongside its Revenue Proposal on 28 February 2007. The AER's Draft Decision, dated 31 August 2007, did not accept SP AusNet's proposed pricing methodology, and the AER required a number of consequential amendments. The AER's consideration of SP AusNet's proposed pricing methodology and the required amendments are set out in Chapter 11 and Appendix F of the Draft Decision.

SP AusNet has reviewed carefully the AER's Draft Decision, and accepts all of the required amendments as presented by the AER in Appendix F of the Draft Decision.

This document is SP AusNet's revised proposed pricing methodology in accordance with clause 6A.12.3(a) of the Rules.

Clause 6A.24.1 of the Rules states that the *pricing methodology*:

(1) allocates the aggregate annual revenue requirement (AARR) for prescribed transmission services to:

  (i) the categories of prescribed transmission services; and

  (ii) transmission network connection points; and

(2) determines the structure of the prices that a Transmission Network Service Provider may charge for each of the categories of prescribed transmission services.

The NER also require that the *pricing methodology* satisfies principles and guidelines established by the NER. In particular, clause 6A.10.1(e) of the NER require that the proposed *pricing methodology* must:

(1) give effect to and be consistent with the *Pricing Principles for Prescribed Transmission Services* (that is to say, the principles set out in rule 6A.23); and

(2) comply with the requirements of, and contain or be accompanied by such information as is required by, the pricing methodology guidelines made for that purpose under rule 6A.25.

For the purposes of this forthcoming regulatory period, SP AusNet is subject to interim arrangements (as opposed to *pricing methodology guidelines*) in accordance with clause 11.8.4 of the NER. The AER issued interim arrangements in February 2007.

The AER's interim arrangements include the following summary of the AER's approach:

> "The AER believes that in lieu of the AER's pricing methodology guidelines, it is appropriate for the relevant provider's proposed pricing methodology to be assessed against the provisions in Part C of Chapter 6 of the NER (as in force immediately before the commencement of the National Electricity Amendment (Economic Regulation of Transmission Services) Rule and as reflected in version 9 of the

> NER), to the extent those provisions are not inconsistent with the pricing principles in Part J of the NER."

SP AusNet has reviewed its previous pricing methodology, which complied with Part C of Chapter 6 of the NER (as in force immediately before the commencement of the National Electricity Amendment (Economic Regulation of Transmission Services) Rule ("Part C of the old Chapter 6"). SP AusNet's view is that its previous pricing methodology is consistent with the pricing principles in Part J of Chapter 6A.

In order to comply explicitly with the pricing principles in Part J of Chapter 6A and the AER's interim arrangements, SP AusNet's previous pricing methodology has been redrafted to reflect the terminology and drafting employed in Part J of Chapter 6A. In respect of matters that do not relate to the pricing principles in Part J of Chapter 6A, SP AusNet's proposed pricing methodology refers to Part C of the old Chapter 6 in accordance with the requirements of the interim arrangements.

It is also important to note that the transmission arrangements in Victoria differ from those in other states, given the roles and responsibilities that are ascribed to SP AusNet and VENCorp. In relation to pricing matters, SP AusNet undertakes the allocation of the *AARR* to each of the *categories of prescribed transmission services*, and is also responsible for pricing *connection services*. VENCorp is responsible for pricing *prescribed TUOS services* and *prescribed common transmission services*.

In light of the arrangements in Victoria, this proposed *pricing methodology* only addresses the pricing matters for which SP AusNet has responsibility. SP AusNet understands that VENCorp will submit its own *pricing methodology* to the AER in accordance with the requirements of the NER.

The remaining sections of this document are structured as follows:

- Section 2 defines the AARR in accordance with the NER.
- Section 3 explains the allocation of the AARR to the categories of prescribed transmission services in accordance with clause 6A.23.2, in order to establish the Annual Service Revenue Requirements (ASRR) for each category.
- Section 4 explains the allocation of the ASRR to transmission network connection points in accordance with clause 6A.23.3.
- Section 5 explains the application of the price structure principles to the charges for connection services in accordance with clause 6A.23.4.
- Section 6 describes the requirements relating to information provision, and the billing arrangements in accordance with clause 6.7 of Part C of the old Chapter 6.

Throughout this document, terms which appear in *italics,* have the meaning given to them in the NER.

2. SP AusNet's Aggregate Annual Revenue Requirement

Clause 6A.22.1 states that for the purposes of the pricing arrangements, the aggregate annual revenue requirement (AARR) for prescribed transmission services provided by a Transmission Network Service Provider, is the maximum allowed revenue referred to in clause 6A.3.1 adjusted:

(1) in accordance with clause 6A.3.2, and

(2) by subtracting the operating and maintenance costs expected to be incurred in the provision of prescribed common transmission services

Clause 6A.3.1 states that the revenue that a Transmission Network Service Provider may earn in any regulatory year of a regulatory control period from the provision of prescribed transmission services is the maximum allowed revenue subject to any adjustments referred to in clause 6A.3.2, and is to be determined in accordance with:

(a) the revenue determination forming part of the applicable transmission determination; and

(b) the provisions of the revenue rules set out in Part C of Chapter 6A, which relates to the regulation of revenue for prescribed transmission services.

In accordance with the requirements of the NER, SP AusNet defines the *AARR* in accordance with clauses 6A.3.1, 6A.3.2 and 6A.22.1. Importantly, clause 6A.3.1 notes that the *AARR* should be defined in accordance with the *revenue determination*. At this stage, the *revenue determination* relating to the forthcoming *regulatory control period* has not yet been settled. However, SP AusNet undertakes to ensure that the *AARR* for price setting purposes is defined in accordance with the *revenue determination*.

3. Allocation of the AARR to Categories of Prescribed Transmission Services

3.1 Overview of Allocation Principles

Clause 6A.23.2 of the NER requires the *AARR* to be allocated in accordance with the following principles:

(a) The AARR for a Transmission Network Service Provider must be allocated to each category of prescribed transmission services in accordance with the attributable cost share for each such category of services.

(b) This allocation results in the *annual service revenue requirement* (*ASRR*) for that category of services.

(c) The allocation of the *AARR* must be such that:

    (1) every portion of the *AARR* is allocated; and

    (2) the same portion of the *AARR* is not allocated more than once.

(d) Where, as a result of the application of the *attributable cost share*, a portion of the *AARR* would be attributable to more than one *category of prescribed transmission services*, that *attributable cost share* is to be adjusted and applied such that any costs of a *transmission system* asset that would otherwise be attributed to the provision of more than one *category of prescribed transmission services*, is allocated as follows:

(1) to the provision of prescribed TUOS services, but only to the extent of the stand-alone amount for that category of prescribed transmission services;

(2) if any portion of the costs of a *transmission system* asset is not allocated to *prescribed TUOS services*, under subparagraph (1), that portion is to be allocated to *prescribed common transmission services*, but only to the extent of the *stand-alone amount* for that *category of prescribed transmission services*;

(3) if any portion of the costs of a *transmission system* asset is not attributed to *prescribed transmission services* under subparagraphs (1) and (2), that portion is to be attributed to *prescribed entry services* and *prescribed exit services*.

Clause 6A.22.3 defines the meaning of *attributable cost share* as follows:

(a) For a *Transmission Network Service Provider* for a *category of prescribed transmission services*, the *attributable cost share* for that provider for that category of services must, subject to any adjustment required under the principles in Clause 6A.23.2, substantially reflect the ratio of:

(1) the costs of the *transmission system* assets directly attributable to the provision of that *category of prescribed transmission services*; to

(2) the total costs of all the Transmission Network Service Provider's transmission system assets directly attributable to the provision of prescribed transmission services.

(b) The costs of the *transmission system* assets referred to in paragraph (a) refers to optimised replacement cost or to an accepted equivalent to optimised replacement cost that is referable to values contained in the accounts of the *Transmission Network Service Provider*.

3.2 Application of the Allocation Principles

In accordance with clause 6A.22.3 SP AusNet determines the *attributable cost share* for each category of *prescribed transmission services* by calculating the ratio of:

(1) the costs of the *transmission system* assets directly attributable to the provision of that *category of prescribed transmission services*; to

(2) the total costs of SP AusNet's *transmission system* assets directly attributable to the provision of *prescribed transmission services*.

In accordance with the requirements of the NER, in calculating the costs referred to above, SP AusNet values its assets in accordance with an optimised replacement cost methodology. Any optimisation will be conducted in accordance the asset valuation roll-forward methodology described in the Rules.

To give effect to the allocation process, assets must be ascribed to the particular *category of prescribed transmission services* in accordance with clause 6A.23.2 of Part J of the NER and

Schedule 6.2 of Part C of the old NER. In the following paragraphs SP AusNet describes how the particular categories of assets have been allocated to *prescribed transmission service categories* by applying the principles set out in clause 6A.23.2 of Part J of the NER and Schedule 6.2 of Part C of the old NER. As already noted, clause 6A.23.2(c)(2) defines the resulting amount of the *AARR* allocated to each of the *categories of prescribed transmission services* as the *annual service revenue requirement* (*ASRR*).

3.1.1 Lines

All lines are allocated to *prescribed TUOS services*, with the following exceptions:

- 66 kV double circuit lines between East Rowville, Cranbourne and Frankston Terminal Stations; and
- 66 kV double circuit lines between Templestowe Terminal Station and Subs DC, HB, L and WD.

In accordance with Schedule 6.2 of Part C of the old NER, the line assets listed immediately above are allocated to *prescribed exit services*, as each of the above lines is radial and connects a particular user to the transmission network.

3.1.2 Transformers

The main system tie transformers are allocated to *prescribed TUOS services*. Connection Transformers are allocated to *prescribed entry services* and *prescribed exit services* in accordance with Schedule 6.2 of Part C of the old NER.

3.1.3 Switchgear

In accordance with Schedule 6.2 of Part C of the old NER, a shallow connection policy is applied in determining the allocation of switchgear. In accordance with this policy, switchgear is assigned to *prescribed entry services* and *prescribed exit services* only when those assets provide *supply* to *Network Users* connected at the *connection point*. The remainder is assigned to *prescribed TUOS services*.

3.1.4 Busbars and Rack Structures

Busbars and rack structures are not separately identified for allocation. Instead, they are included in the relevant switchgear, transformer or reactive primary bays.

3.1.5 Reactive Compensation Plant

In accordance with Schedule 6.2 of Part C of the old NER, all reactive plant is assigned to *prescribed common transmission services* as it provides equivalent benefit to all users.

Reactive plant will be assigned to *prescribed TUOS services* if the benefits of the reactive plant can be allocated on a locational basis, but cannot be allocated to a particular user or group of users.

Reactive plant at the sub-transmission voltage level will be assigned to *prescribed exit services* if it is clearly evident that the plant has been provided to meet the local reactive requirements of one or more users connected at the relevant substation.

3.1.6 Land and Station Establishment

Land and establishment costs are apportioned between *prescribed exit services* and *prescribed TUOS services* on a case-by-case basis applying the principles set out in clause 6A.23.2.

3.1.7 Communications

All communication assets are assigned to *prescribed common transmission services*.

3.1.8 Secondary Systems

Secondary equipment is generally allocated in accordance with the allocation of the associated primary equipment.

3.1.9 Victorian Network Switching Centre

All operational costs are assigned to *prescribed common transmission services*.

3.1.10 System Spares

System spares are allocated to prescribed common transmission services.

3.1.11 Non-System Assets

Non-system assets are allocated to prescribed common transmission services.

3.1.12 Easements

Easements are allocated to prescribed common transmission services.

3.1.13 Easement Land Tax

On 24 March 2004 the Victorian Government announced that it intended to extend land tax to electricity easements owned by electricity transmission companies in Victoria. Legislation to give effect to the changes, entitled the *Land Tax (Amendment) Act 2004*, received royal assent on 27 April 2004.

As the tax is directly associated with value of the easement portfolio, SP AusNet intends to allocate this cost to the prescribed common transmission services.

4. Allocation of the ASRR to Transmission Network Connection Points

4.1 Overview of Allocation Principles

As noted earlier, the allocation process described in section 3 results in the allocation of SP AusNet's *AARR* to each *category of prescribed transmission service*. This allocation is defined in the NER as the *annual service revenue requirement* (*ASRR*).

This section of SP AusNet's proposed *pricing methodology* explains how the *ASRR* for *prescribed entry* and *exit services* is to be allocated to transmission network connection points. It should be noted that VENCorp is responsible for allocating the *ASRR* for *prescribed TUOS services* and *prescribed common transmission services* in accordance with the NER.

Clause 6A.23.3 sets out the following principles for allocating the ASRR to *transmission network connection points:*

(a) The whole of the ASRR for prescribed entry services is to be allocated to transmission network connection points in accordance with the attributable connection point cost share for prescribed entry services that are provided by the Transmission Network Service Provider at that connection point.

(b) The whole of the ASRR for prescribed exit services is to be allocated to transmission network connection points in accordance with the attributable connection point cost share for prescribed exit services that are provided by the Transmission Network Service Provider at that connection point.

Clause 6A.22.4 defines the attributable connection point cost share as follows:

(a) For a Transmission Network Service Provider for prescribed entry services and prescribed exit services, the attributable connection point cost share for that provider for each of those categories of services must substantially reflect the ratio of:

    (1) the costs of the transmission system assets directly attributable to the provision of prescribed entry services or prescribed exit services, respectively, at a transmission network connection point; to

    (2) the total costs of all the Transmission Network Service Provider's transmission system assets directly attributable to the provision of prescribed entry services or prescribed exit services, respectively.

(b) The costs of the *transmission system* assets referred to in paragraph (a) refers to optimised replacement cost or to an accepted equivalent to optimised replacement cost that is referable to values contained in the accounts of the *Transmission Network Service Provider*.

4.2 Application of the Allocation Principles

In accordance with clause 6A.23.3 SP AusNet allocates the ASRR for prescribed entry and exit services to be transmission network connection points in accordance with the attributable connection point cost share for prescribed entry and exit services at each connection point by calculating the ratio of:

(1) the costs of the transmission system assets directly attributable to the provision of prescribed entry services or prescribed exit services, respectively, at a transmission network connection point; to

(2) the total costs of all SP AusNet's *transmission system* assets directly attributable to the provision of *prescribed entry services* or *prescribed exit services*, respectively.

In accordance with the requirements of the NER, in calculating the costs referred to above, SP AusNet values its assets in accordance with an optimised replacement cost methodology. Any optimisation will be conducted in accordance the asset valuation roll-forward methodology described in the NER.

The NER do not specify any principles to address the allocation of costs to multiple customers at a single terminal station. Nevertheless, SP AusNet proposes the following standard allocation methodology for multiple customers at a single terminal station with its existing customers. Customers remain free to negotiate a different methodology with SP AusNet at any time.

4.2.1 Shared Entry Services

Where more than one entry customer shares a terminal station, shared costs will be allocated by asset replacement costs (ORC) share. An example showing the breakdown of assets undertaken in accordance with clause 2.2(a)(1) of the interim arrangements at an entry terminal station is illustrated in Appendix 1 attached to this proposed pricing methodology.

4.2.2 Shared Exit Services

Where more than one exit customer is supplied from a terminal station, shared costs will be allocated under the following methodology:

- Coincident maximum demand (average of 10 highest demand days) will be used to determine the allocation of costs between customers at shared exit terminal stations. Adjustments to the coincident maximum demand will be made where a feeder is shared between two of more customers. This information and any adjustments necessary will be agreed by all customers at the relevant connection point;
- Coincident maximum demand information provided for the allocation will be for the previous financial year. For example, in the calculation of the 2007 / 08 charges, data from 2006 / 07 would be used; and
- The proportion of shared costs allocated to a new exit customer must be calculated on the basis of a reasonable estimate of expected demand (over a period of not less than six months), consistent with the terms of the connection agreement between SP AusNet and the new exit customer.

SP AusNet will receive the required information from the relevant *Distribution Network Service Provider* as a percentage split for each shared terminal station. Non-distributor connection customers will have identical consultation opportunities and be subject to identical allocation principles.

An example showing the breakdown of assets undertaken in accordance with clause 2.2(a)(1) of the interim arrangements at an exit terminal station is illustrated in Appendix 2 attached to this proposed pricing methodology.

4.2.3 Shared Exit and Entry Services

Where an exit customer shares a terminal station with a *Generator* or *MNSP*, shared costs will be allocated by asset optimised replacement cost (ORC) share.

5. Price Structure

Clause 6A.23.4 requires each *TNSP* to develop separate prices for the recovery of the *ASRR* in accordance with the principles set out in paragraphs (b)-(i). As noted earlier, SP AusNet is responsible for the pricing of *prescribed entry* and *exit services* only, whilst VENCorp has responsibility for pricing *prescribed TUOS services* and *prescribed common transmission services*.

In relation to *prescribed entry* and *exit services*, clause 6A.23.4(c) requires that prices for *prescribed entry services* and *prescribed exit services* must be a fixed annual amount. In accordance with this NER requirement, SP AusNet therefore proposes that prices for *prescribed entry* and *exit services* are fixed annual amounts.

6. Information Requirements and Billing

6.1 Compliance with Part C of the Old Chapter 6

In accordance with the interim arrangements, SP AusNet is required to adopt the billing process requirements set out in Part C of the old Chapter 6, rather than those in clause 6A.27 of Part J of Chapter 6A.

6.2 Timing

Clause 6.5.7(a) requires each *TNSP* to publish transmission service prices for the following *financial year*, by 15 May each year. In accordance with this requirement, prices for *prescribed entry* and *exit services* will be determined and issued by 15 May of the relevant *financial year*.

The *ASRR* for *prescribed TUOS services* and *prescribed common transmission services* for the following *financial year* will be issued to VENCorp two weeks before 15 May to allow VENCorp to calculate the prices for these services in accordance with the Rules by 15 May.

6.3 Information requirements from customers

Customers should provide SP AusNet with the required Maximum Demand information (described in section 4.2 above) and any adjustments as agreed by all relevant parties by the last business day of April.

6.4 Statement of charges to connection customers

In accordance with the relevant sections of clause 6.7.2 of Part C of the old Chapter 6, SP AusNet will issue a statement outlining the annual connection charge by 15 May. The statement will contain the following information:

- the total connection charge;
- the breakdown of the connection charge by each customer connection point;
- the dates on which the billing period starts and ends; and
- any relevant measured quantities, agreed quantities, prices and amounts charged for each component of the *Generator's* or *Transmission Customer's* total connection service account.

6.5 Statement of Charges to VENCorp

SP AusNet will endeavour to issue a statement outlining the annual transmission service charge payable by VENCorp two weeks before 15 May. The statement will contain the following information:

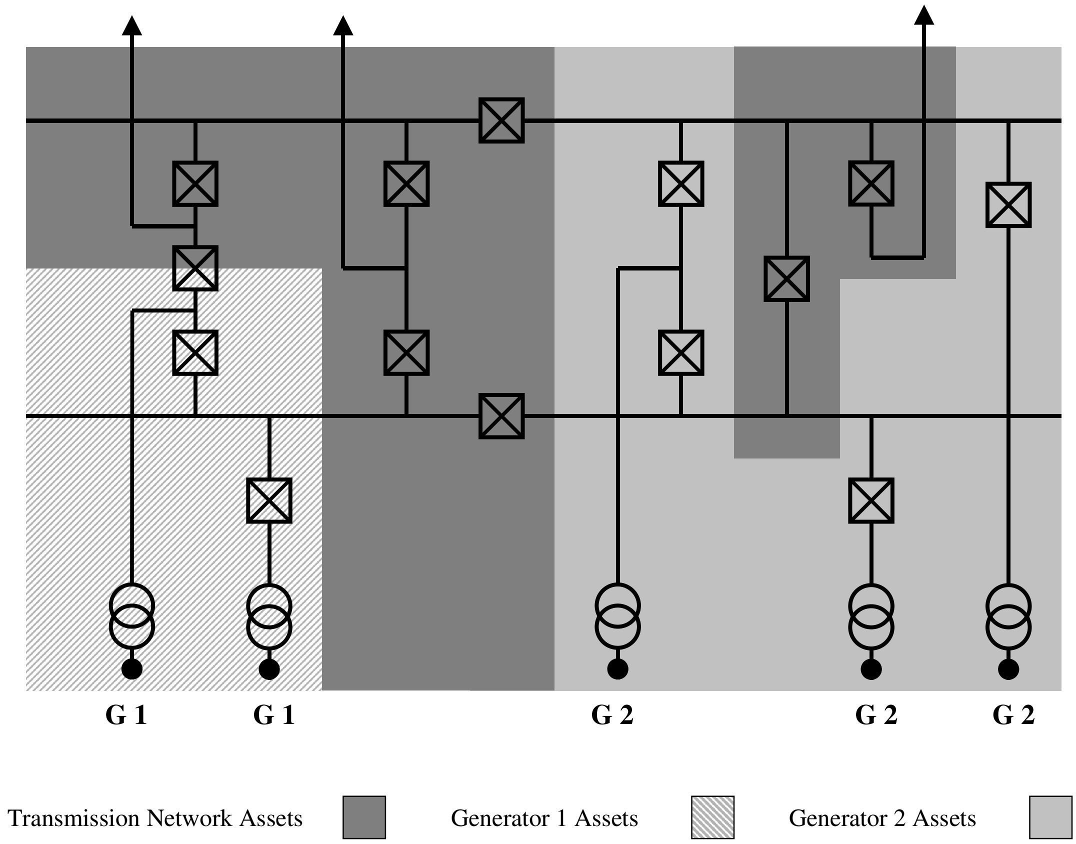
- the *AARR*;
- the breakdown of the *AARR* into the *ASRRs* to enable VENCorp to determine the pricing of *prescribed TUOS services* and *prescribed common transmission services*; and

- any relevant measured quantities, agreed quantities, prices and amounts charged for each component of VENCorp's total annual transmission service fee.

6.6 Billing Frequency and Settlement

The annual transmission service fee payable by VENCorp and the connection charges payable by Transmission Customers will be recovered via twelve monthly bills issued one month in arrears. Settlement is 11 business days from the date of issue.

Appendix 1 – Shared Entry Terminal Station Example



Appendix 2 – Exit Terminal Station Example