



21 January 2010

Mr Mike Buckley  
General Manager  
Network Regulation North Branch  
Australian Energy Regulator

c/o aerinquiry@aer.gov.au

Dear Mr Buckley

**Re: SSROC Submission on EnergyAustralia's Submission for the AER's  
Redetermination of Public Lighting Prices 2010 to 2014**

Thank you for the opportunity to comment on EnergyAustralia's Submission for the AER's Redetermination of Public Lighting Prices 2010 to 2014. As with previous submissions to the AER, the Southern Sydney Regional Organisation of Councils (SSROC) makes this submission on behalf of 34 Councils participating in the SSROC Street Lighting Improvement Program and constituting approximately 94% of all EnergyAustralia street lights.

**A LARGE AMOUNT OF INCOMPLETE INFORMATION**

**At the outset, SSROC notes that despite filing over 2400 pages of submittals, EnergyAustralia has withheld from SSROC and Council review the underlying pricing model, and many of the underlying assumptions. It is simply not possible to address many of EnergyAustralia's claims in the absence of this basic information.**

As was noted by the Australian Competition Tribunal, "...upon setting aside the determination of the AER, a detailed consideration of spreadsheet modelling and an awareness of the interaction of any changes will be required."<sup>1</sup>

That Councils, who were legitimately accepted as a party to the Tribunal process, are excluded from detailed consideration of the price modelling on which any revised pricing proposal is based is entirely inappropriate, inconsistent with the Tribunal discussion of a "...proper opportunity for the making of submissions on the issues by EA and SSROC..."<sup>2</sup> and continues the pattern by EnergyAustralia of withholding such information from proper consideration by Councils, the parties most directly affected by the pricing review process.

<sup>1</sup> Australian Competition Tribunal, Application by EnergyAustralia AcompT 7, 16 Oct 2009, Section 27

<sup>2</sup> ibid, Section 38

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As previously stated in SSROC submissions, street lighting is an essential but monopoly service and as such, there should be absolute transparency on the costing models that a decision on efficient costs is to be based on. SSROC notes the significant difference between information access provided in the case of EnergyAustralia street lighting and that found in the review of Victorian street lighting pricing currently ongoing at the AER as part of the Victorian DNSP network pricing review.

## **SCOPE OF ENERGYAUSTRALIA REDETERMINATION SUBMISSION**

**Taken in total, the 2,400 pages of submissions and supporting documents EnergyAustralia has submitted to the AER amounts to a recommencement of the street lighting pricing determination process. EnergyAustralia's submission is by no means a focussed correction of errors, but an attempt to recommence the pricing review. As such it is surely inconsistent with the Tribunal's objective, and is certainly inconsistent with the two-week review period offered to Councils during a period in which NSW Councils do not meet.**

SSROC considers that EnergyAustralia has greatly exceeded the bounds set by the Tribunal for the redetermination process. Specifically, a recommencement is at variance with Section 32 of the Tribunal decision of 16 October 2009, where the Tribunal states that, *"Ideally, the end result [of remittal] should not require a recommencement of the entire process undertaken previously by the AER. The object of the remittal is to correct errors, leaving the AER to re-determine any aspects of the determination set aside which have not been singled out by the Tribunal as being in error. However, once the determination is set aside, if the AER is persuaded of error, other than that identified by the Tribunal, the AER has the power and the duty to correct that error in its re-determination."*<sup>3</sup>

Disclosure and scope issues aside, SSROC has the following preliminary comments on the material that has been provided in EnergyAustralia's submission of 7 January 2010:

### **ENERGYAUSTRALIA SUBMISSION SECTION 2: Proposed Revisions to Regulatory Asset Base**

EnergyAustralia is seeking \$31m upward adjustment in the RAB as determined by the AER in its Final Decision. Notably, the Tribunal did not find the AER's decision on the RAB to be in error and stated only that the AER may reconsider this issue.

There are a number of important reasons why EnergyAustralia's proposed major RAB revision including the basis on which it was calculated should be rejected:

- a) **Deferred Depreciation** – EnergyAustralia has provided considerable new discussion on a claim for deferred depreciation. SSROC reserves its right to make additional comment on this specific issue but notes in the interim that IPART's 2005 decision makes no explicit reference to substantial deferred depreciation and clearly states that full cost recovery would be achieved by the end of the regulatory period. While IPART's letter of 10 December 2009 confirms the 2004 RAB assumed by EnergyAustralia in the last pricing decision, **IPART does not explicitly endorse EnergyAustralia's claim of substantial deferred depreciation despite this having been requested by EnergyAustralia.**

Substantiating the case that EnergyAustralia had been front loading depreciation, IPART again confirms that it accepted the conclusions of Wilson Cook's 2005 report which found that that historic capex had been *"below sustainable levels"*<sup>4</sup> for some time with a

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<sup>3</sup> ibid Section 32

<sup>4</sup> Wilson Cook Review of EnergyAustralia Public Lighting Expenditure August 2005, p1

*“lack of replacement expenditure in the period 1999 to 2004 in comparison with the depreciation charge taken”<sup>5</sup>. Wilson Cook also concluded that asset life assumptions by EnergyAustralia were inappropriately short for some assets and went on to acknowledge that capex in the next regulatory period would rise due to the need to replace large number of “unreliable”<sup>6</sup> T8\*20 fluorescent luminaires with this one program alone making up more than half of all planned capex (see items D and E below on misinvestment).*

- b) **Contributed Assets** – In real terms, a sinking fund required to accumulate enough to replace a \$100 asset having a 20 year life would only require an annual contribution of about \$2 per year. This remains the case, even if the piece of equipment has been replaced multiple times over many decades (eg a perpetual sinking fund).

In contrast, if an asset with a life of 20 years has been funded by a party other than the customer and a return on and return of capital is required, the annual payment by the customer would be more than five times the annual contribution required for a sinking fund.

In summary, what matters in terms of capex contributions for an asset that is to be perpetually replaced is who **FIRST** paid for the asset at the time that the initial asset was installed.

In EnergyAustralia’s case, more than 95% of EnergyAustralia’s public lighting assets were in recent years classified as ‘Rate 1’ which broadly has the same definition as the AER’s Tariff Class 1. Of note is that:

- The fundamental assumption behind EnergyAustralia’s ‘Rate 1’ tariff is that the original capital for lighting at that point was provided by EnergyAustralia<sup>7</sup>. The assumption that EnergyAustralia provided the original capital for these installations is a key element contributing to the high RAB claimed by EnergyAustralia.
- In contrast to EnergyAustralia’s unsupported assumption, the vast majority of lighting points on EnergyAustralia’s well established network, where the first lights were installed more than 100 years ago, were in fact **FIRST** lit by Council Electricity Departments or by County Councils in the decades prior to the creation of corporatised electricity companies such as Sydney Electricity (1990) and Shortland Electricity (1993).
- In most cases, the ORIGINAL capital was thus provided by Councils or the Country Councils they owned and managed.
- At corporatisation, NO compensation was paid to Councils for the assets (including the public lighting assets) transferred from the County Councils to the new State-owned entities.

Councils submit that there is a material question about which party actually provided the original capital for the vast bulk of lighting installations in the EnergyAustralia distribution territory and thus the appropriateness of key assumptions underlying the claimed RAB.

Councils will press this issue over the coming weeks with a review of archives to document arrangements under which the County Councils were amalgamated.

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<sup>5</sup> *ibid*, p15

<sup>6</sup> *ibid* p8

<sup>7</sup>[http://www.energy.com.au/energy/ea.nsf/AttachmentsByTitle/Public+Light+Price+List+Jul+07/\\$FILE/Public\\_Light\\_Price\\_List\\_1Jul07.pdf](http://www.energy.com.au/energy/ea.nsf/AttachmentsByTitle/Public+Light+Price+List+Jul+07/$FILE/Public_Light_Price_List_1Jul07.pdf)

- c) **IPART 1999 RAB an Inappropriate Sole Starting Point** - IPART's review of public lighting in previous decisions was 'light handed', limited to accepting or rejecting EnergyAustralia's proposal and, "IPART was not required to determine building block assumptions"<sup>8</sup> in setting the RAB. Rather, the RAB used by IPART was set by an amount removed from the EnergyAustralia prescribed RAB in a previous regulatory decision in 1999<sup>9</sup> without detailed consideration as to the specifics of EnergyAustralia's street lighting asset base.

To lock in this figure in perpetuity as a 'line in the sand' without opportunity for reconsideration by the AER seems unsupportable given the acknowledged limits to IPART's remit at the time, the subsequent detailed consideration by the AER of many underlying RAB assumptions and subsequent changes in circumstances.

- d) **Material Misinvestment By EnergyAustralia Not Considered** - Further undermining a claim for a higher RAB is significant evidence of misinvestment by EnergyAustralia over a period of up to two decades which has not been considered in EnergyAustralia's revised RAB proposal despite EnergyAustralia's response to this situation being a key aspect of EnergyAustralia's revised pricing proposal in the 2004/05 IPART pricing review.

As per previous SSROC submissions and as expanded on below, Councils' position is that most EnergyAustralia tubular fluorescent installations (eg TF2\*20, TF1\*40 and other obsolete fluorescent variants) are the result of long-term and large-scale misinvestment by EnergyAustralia in the post-1985 period. A similar case can be made with respect to the continued installation of high wattage mercury vapour (eg MV250, MV400 and MV700) on main roads long after the use of this inefficient technology had ceased elsewhere.

In summary, EnergyAustralia has had responsibility to ensure that the lighting technology practices were efficient and current for decades. Historically, councils have had little say on technology selection, and have been dependent on EnergyAustralia for performing public lighting services efficiently. However, as discussed in the following points, EnergyAustralia failed to meet its obligations in this regard in the case of several types of lighting constituting more than half its total inventory at the beginning of the last regulatory period:

- In EnergyAustralia's Supplementary Response to the AER on public lighting<sup>10</sup> the company stated that its approach to technology selection had "*...been to evaluate and install luminaires that would avoid a maintenance regime that would increase cost of service to public lighting customers and decrease the effectiveness of public lighting to the community*". This statement is consistent with lighting contracts that existed in past decades which specified that EnergyAustralia would "*...keep the lamps and all appliances...efficient and reasonably in accordance with the latest improvements*"<sup>11</sup> and statements that EnergyAustralia "*...has been exercising a close control over all aspects of costs with a view to minimising price increases.*"<sup>12</sup>
- The TF 2\*20W and similar luminaires was developed in about 1958-1959 and its optical characteristics and performance changed little over subsequent decades.

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<sup>8</sup> IPART Letter to EnergyAustralia 10 December 2009

<sup>9</sup> IPART Letter to EnergyAustralia 2 March 2005

<sup>10</sup> Response to Submissions on EnergyAustralia's Public Lighting Proposal, 30 October 2008, p11

<sup>11</sup> PBA "EnergyAustralia Streetlighting Cost to Serve" 16 October 2003, p. 28

<sup>12</sup> Sydney Electricity letter to councils, 27 June 1991

- As per a report on Australian public lighting conducted for the Australian Greenhouse Office, *“Until about 1985, 2\*20W and 40W fluorescent lamps were the common choices [on residential roads in Australia].”*<sup>13</sup>
- However, by the mid 1980’s, 2\*20W and 40W fluorescent luminaires were acknowledged to have high overall costs due to high outage rates.
- Recognising this, most Australian utilities discontinued new installations in the mid 1980s and, in the case of Victoria, the SECV began a pro-active bulk removal program for TF2\*20 luminaires in the mid 1980s which is understood to have been largely complete by about 1990.
- Evidence of the high outage rates and consequent high cost maintenance regime required for the TF2\*20 is to be found in EnergyAustralia’s bulk lamp replacement cycle on residential roads which, until about 2005, needed to be 18 months to cope with the requirements of the large population of TF2\*20 luminaires on the EnergyAustralia network<sup>14</sup>.
- EnergyAustralia only discontinued installing TF2\*20 lighting after July 2004 when Councils, having independently been made aware of the consequences, jointly wrote to EnergyAustralia insisting installations be stopped (along with installations of obsolete high wattage mercury vapour luminaires on main roads –see below)
- TF2\*20W lighting does not currently and has not for many, many years complied with key aspects of AS1158.3.1, the lighting standard for residential roads in Australia.
- With respect to lighting effectiveness, the TF2\*20W delivered lighting to the absolute minimum lighting level in AS1158 to about 15m either side of the pole. It was thus impossible to comply with the minimum required lighting levels in AS1158 over more than 30m or less than half of what was needed at an absolute minimum. Indeed, the average spacing of EnergyAustralia’s lights on residential roads is perhaps 66m based on a historic practice going back at least eight decades of installing a light on every second distribution pole in the former Sydney County Council distribution area (and elsewhere in Australia).
- On those occasions in which some council input was involved in lighting selection, Councils generally requested and relied on EnergyAustralia advice that in hindsight was often incomplete and incorrect. For example, Councils regularly receive requests from the public for additional lighting to be installed. In those cases, the normal practice was for the Council to refer the request to EnergyAustralia, seeking advice as to whether and what type of new luminaire would be appropriate. EnergyAustralia regularly recommended use of additional TF2x20s up to July 2004.<sup>15</sup> Furthermore, it should be noted that EnergyAustralia also continued to encourage the use of TF2x20s through prices which were lower than those for the better performing mercury luminaires widely used by other Australian utilities from the mid 1980s, and indicating that such cost differences were cost-reflective.<sup>16</sup> Historical pricing, based on poor cost analyses, continually and inappropriately encouraged councils to accept TF2x20s.

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<sup>13</sup> Public Lighting in Australia – Energy Efficiency Challenges and Opportunities Final Report 2005, Dept of the Environment and Heritage, Australian Greenhouse Office, p19

<sup>14</sup> As per EnergyAustralia briefings to SSROC in 2004/05 on a review of the BLR cycle

<sup>15</sup> e.g., general design guidance provided in a letter from EnergyAustralia to Sutherland Shire Council, 16 April 1997; and numerous specific examples, e.g., EnergyAustralia, letter to Burwood Council, 8 September 2003.

<sup>16</sup> e.g., Sydney Electricity, letter to Marrickville Council, 12 May 1995 in response to a query regarding the most cost efficient and lowest cost lighting solution for residential streets.

- A similar case of misinvestment exists for the continued deployment of high wattage mercury vapour lighting (eg MV250, MV400 and MV700) by EnergyAustralia on main roads long after new installations of this lighting type had ceased elsewhere. As per the last consolidated EnergyAustralia inventory supplied to Councils in 2007, more than 41,000 main road lights were high wattage mercury vapour luminaires. This obsolete technology thus constituted approximately 60% of EnergyAustralia's main road lighting network. Excluding EnergyAustralia's asset mix from the data, this is fully double the national average of other Australian utilities where the residual population of mercury vapour on main roads was some 29% of total main road lighting in 2004 and has been progressively declining since. As is clear from the national figures, EnergyAustralia also failed to maintain technical currency with regards to main road lighting technology.
- At least the last decade of high wattage mercury vapour installations on main roads by EnergyAustralia constitute a clear case of misinvestment. Notably, high wattage mercury vapour lighting on main roads has energy consumption 33% higher than the high pressure sodium technology that replaced it with consequent higher energy and network distribution costs for Councils as a result of this misinvestment.
- By comparison, Integral Energy has not claimed to have ANY residual populations of obsolete tubular fluorescent lighting nor of high wattage mercury vapour lighting. As such, it did not seek a price for TF2\*20, TF40, M250, MV400 or MV700 lights in the AER pricing review<sup>17</sup>.

The clear pattern of misinvestment by EnergyAustralia described above and substantiated by the very different inventory mix held by EnergyAustralia as compared to other utilities should be given full consideration in the context of EnergyAustralia's requested RAB revision. Indeed, it strongly supports the AER's contention that a substantive readjustment of the claimed RAB was in order.

- e) **Cancelled Accelerated Replacement Program Missing from RAB Consideration -** EnergyAustralia's 2004/05 revised pricing submission was based in part on an accelerated replacement of large numbers of obsolete tubular fluorescent lights in a \$30 million capital replacement program over 7-8 years<sup>18</sup>. This program has only been partly completed and has been dropped from consideration by EnergyAustralia in submissions to the AER post June 2008 including the current submission.

As originally proposed by EnergyAustralia, this program involved accelerated replacement of some 105,000<sup>19</sup> obsolete and poorly performing tubular fluorescent luminaires (see previous item) at a rate of approximately 15,000 luminaires per year or up to 300% higher than the normal rate of asset replacement.

EnergyAustralia's major capital expenditure program of obsolete assets covering what was then just under half the asset inventory was interpreted by Councils as an implicit acceptance of misinvestment by EnergyAustralia and, in any other accounting context, would most properly have been dealt with as a major asset write-down. No other reasonable interpretation seems plausible. That this major capex program is now dropped from consideration without a substantive corresponding downward adjustment to the RAB is wholly inappropriate. Again, this supports the AER case that

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<sup>17</sup> AER Final Decision p 636-638

<sup>18</sup> EnergyAustralia's Revised Public Lighting Proposal to IPART, June 2005, 11 and EnergyAustralia's Supplementary Submission to IPART on its Public Lighting Pricing Proposals, February 2005, p 4.

<sup>19</sup> Based on summary inventory supplied by EnergyAustralia to Councils in 2004

reconsideration of the RAB originally submitted by EA was in order.

It would be inequitable to now reward EnergyAustralia for this past misinvestment by approving drastic RAB revisions without adequate consideration of this now cancelled asset replacement program. It would do this by removing any future incentive to invest wisely (eg because any misinvestment could be fully recovered from Councils).

f) **Low Labour Productivity Assumptions a Major Contributor to High RAB** - Assumptions about installation labour are a significant contributor to capex assumptions in street lighting. Importantly:

- EnergyAustralia's RAB assumptions are based on historical labour productivity assumptions that were in large part rejected by the AER Final Decision;
- when challenged by EnergyAustralia, the AER's alternative labour assumptions were NOT found to be in error by the Tribunal;
- that the AER found EnergyAustralia's street lighting labour costs are high by comparison with peers is supported by past reviews where, for example, "*A previous SKM survey of a selection of Australian distribution businesses indicates that EA's streetlight maintenance costs are relatively high by industry comparison.*"<sup>20</sup>;
- while EnergyAustralia has not provided its capex labour assumptions in the material released as part of the redetermination, in the 2004/05 pricing review, Councils were informed that EnergyAustralia labour assumptions in its pricing model were 2.3 hours x 2 persons for lights on main roads and 1 hour x 2 persons for installations on residential roads. These labour assumptions used by EnergyAustralia appeared to be markedly higher than those determined in Victorian ESC 2004 pricing review. The significant differences in historic labour assumptions are material, and warrant detailed examination in the context of a request to radically revise the RAB for EnergyAustralia; and
- in the last major pricing review in 2004/05, EnergyAustralia's labour assumptions for luminaire replacements were based on those replacements happening on a spot basis over a distributed area. In contrast, up to 40,000 luminaire replacements<sup>21</sup> made by EnergyAustralia on residential roads since the last pricing review were actually done on a bulk basis (eg single crews doing up to 30 replacements in a day in a contiguous area). Indeed, it appears that well over half of all replacements undertaken during the past regulatory period were done on a bulk basis. However, tariff structures and assumed labour inputs in claimed capital expenditure are based on these having been done on a 100% spot replacement basis. **A 100% spot replacement assumption is therefore an incorrect starting point for assumed labour inputs to tariffs, to assumed street lighting capital expenditure and in setting the RAB.** Notably, the November 2008 ESC Energy Efficient Public Lighting Charges – Draft Decision, is based on a bulk luminaire replacement approach and as such provides useful benchmarks for more appropriate labour assumptions.

### **ENERGYAUSTRALIA SUBMISSION SECTION 3: Proposed Revisions to Operating Expenditure**

EnergyAustralia is seeking \$3.08m upward adjustment in the allowed annual operating expenditure from that determined by the AER in its Final Decision.

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<sup>20</sup> SKM Report on EnergyAustralia's Forecast Operating Cost Program, April 2003, Section 11.5.5.3, Page 71

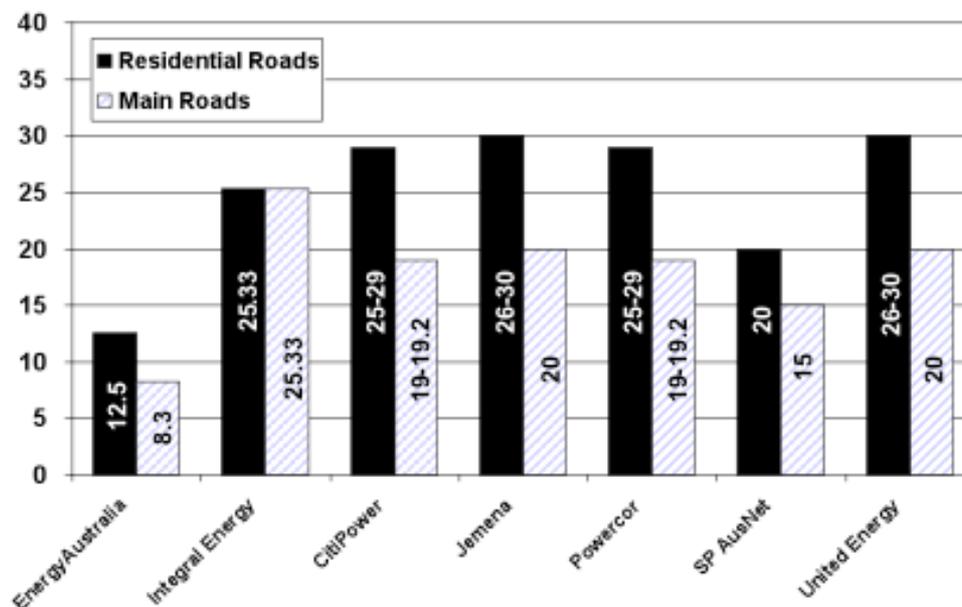
<sup>21</sup> EnergyAustralia Accelerated Replacement Program of obsolete tubular fluorescent lighting with SLA Suburban 80W MBFs with new lighting separately identified in EnergyAustralia inventories

Councils will welcome EnergyAustralia’s acceptance that revisions to its bulk lamp replacement schedule and assumed component failure rates are in order. However, revisions to labour assumptions also warrant reconsideration.

Labour assumptions are at the core of O&M costs. In its redetermination submission to the AER, EnergyAustralia cites a variety of interim submissions to the ESCV’s 2003-04 review of public lighting service charges as proported evidence that the ESCV labour assumptions were not credible. Notably, EnergyAustralia does not cite the ESCV’s final decision which took into account the DNSP submissions nor does it consider the 30 November 2009 submissions by the five Victorian DNSPs to the current 2011-2015 AER pricing review.

The figure below compares spot maintenance assumptions as submitted by Victorian DNSPs in November 2009<sup>22</sup>, Integral Energy’s labour assumptions as approved by the AER in April 2009<sup>23</sup> and EnergyAustralia’s spot maintenance assumptions<sup>24</sup> as per its redetermination proposal. **Overall it can be seen that, on average, other utilities are assuming labour productivity in completing repairs at approximately twice that of EnergyAustralia.**

**Street Lighting Labour Productivity Assumptions:**  
*Lighting Repairs / Day by a 2-person crew in urban areas*



One key aspect of EnergyAustralia’s labour productivity assumptions is travel times. In its redetermination submission (p35), EnergyAustralia makes reference to maximum travel distances in various regions. This discussion presents a misleading picture as it is average travel distances between efficiently scheduled repairs that are of relevance across a large portfolio on the overwhelmingly urban electricity network of EnergyAustralia.

<sup>22</sup> CitiPower, Jemena, Powercor, SP AusNet and United Energy PL Models 2011-2015 as submitted to the AER November 2009, Worksheet: ‘DNSP Inputs O & M’

<sup>23</sup> As per AER Final Decision, April 2009

<sup>24</sup> Per Section 3 of EnergyAustralia’s redetermination submission, 40 minutes total repair time per 2 person crew over an 8.33 hour day with a 3 person crew assumed on average on Traffic Routes, p32-35

In the 2004/05 pricing review, Councils were informed that EnergyAustralia's standard assumption was an average 40 minutes of travel time between jobs<sup>25</sup>. This is consistent with EnergyAustralia's redetermination submission. An average travel time of 40 minutes per repair represents a material logistical inefficiency on the part of EnergyAustralia on the following consideration of average travel distances between repairs:

- In the SSROC area, encompassing 16 Councils from inner Sydney to the outer southern boundary of EnergyAustralia's network there are approximately 108,000 lights<sup>26</sup> in an area of approximately 417 sq km<sup>27</sup>. Average lighting density is thus just over 250 lights per sq km.
- Councils understand that EnergyAustralia undertakes an average of 17,000 spot repairs per year<sup>28</sup> or repairs on about 6.9% of its portfolio.
- As an approximation, EnergyAustralia repairs an average of 17.27 lights in each square kilometer of urban service territory per year.
- There would therefore be, on average, one repair per week in each 3 sq km area assuming an efficiently scheduled weekly service run (the area would be even smaller if pushed to the maximum 8 working days of allowable average repair time under the NSW Public Lighting Code).
- The average distance between efficiently scheduled repairs is thus about 1.73 km.

Even allowing for reasonable set-up times, an assumption of 40 minutes travel time between repair or replacement jobs appears greatly excessive.

EnergyAustralia's overall O&M charges for FY2010 appear high compared to FY2011 price proposals made by Victorian DNSPs in the current AER review<sup>29</sup>. The figure below illustrates O&M pricing proposals by EnergyAustralia in its redetermination submission for four key lighting types as compared to the average price proposed by Victorian DNSPs. Notably, the greatest differences are in minor road lighting which accounts for approximately 70% of all lights in EnergyAustralia's lighting portfolio. The differences would be even greater if the figures were adjusted for inflation.

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<sup>25</sup> EnergyAustralia briefing for SSROC 8 December 2003

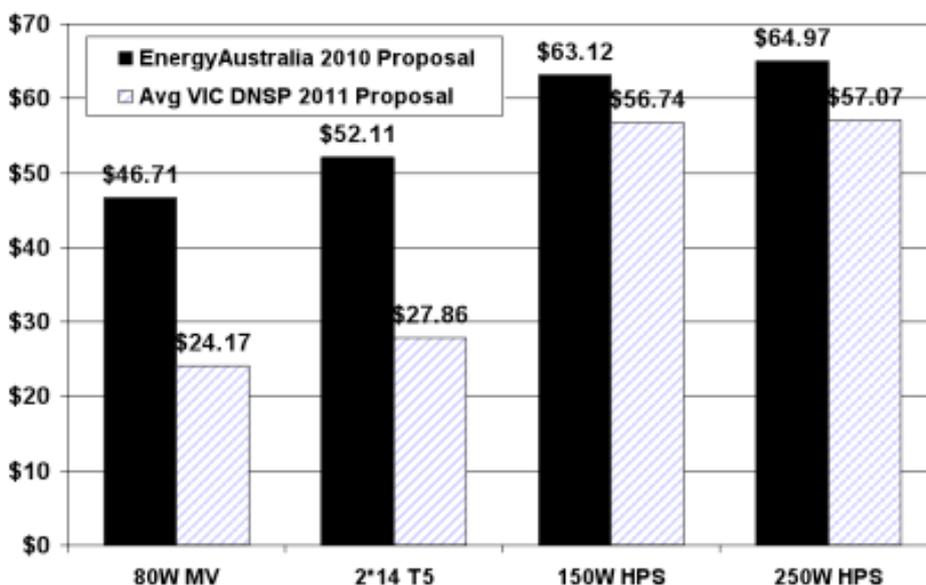
<sup>26</sup> Based on EnergyAustralia supplied inventories

<sup>27</sup> [http://www.dlg.nsw.gov.au/dlg/dlghome/dlg\\_LocalGovDirectory.asp?index=1&CN=ALL#52](http://www.dlg.nsw.gov.au/dlg/dlghome/dlg_LocalGovDirectory.asp?index=1&CN=ALL#52); Excluding areas of bushland in the Sutherland Shire that are unserved.

<sup>28</sup> Based on total repairs reported to SSROC by EnergyAustralia for 2006/07

<sup>29</sup> CitiPower, Jemena, Powercor, SP AusNet and United Energy PL Models 2011-2015 as submitted to the AER November 2009, Worksheet: 'O & M 2011-2015'

## Street Lighting O&M Prices / Year for Key Lights: EnergyAustralia 2010 Proposal vs VIC DNSPs 2011 Proposals



### ENERGYAUSTRALIA SUBMISSION SECTION 4: Residual Value

EnergyAustralia is seeking to have the AER accept a fundamental change to the residual valuation mechanism for assets replaced early. The Tribunal however, did NOT find that the mechanism adopted by the AER in its Final Decision on this matter was fundamentally incorrect, only that it was not sufficiently clear or specific enough.

On this basis, SSROC strongly disagrees with EnergyAustralia's proposed alternative mechanism. In summary, EnergyAustralia is proposing using RAB-derived values of assets being replaced instead of the depreciated original cost of the asset adopted by the AER in its Final Decision.

While EnergyAustralia's proposed approach would create price transparency and certainty, it would do so at a far higher price than is appropriate or was envisioned by the AER. In short, it would greatly overcharge customers by using written-up values for substantially depreciated assets. At its core, there are three key problems associated with EnergyAustralia's proposal:

- It would be inappropriate for a customer to be required to reimburse the residual value of the component being replaced based on an arbitrary assumed remaining life of the population of similar assets. Such an assumption would have no link whatsoever to individual assets that may be 1 or 19 years old and on which Councils may already have paid substantial depreciation. As correctly identified by the AER, the real age (or best available estimate) of the asset should be used to calculate the stranded cost. This is particularly important as most assets to be replaced 'early' are likely to be in the second half of their useful life.
- It would be inappropriate for a customer to be required to reimburse the residual value of the component being replaced based on the RAB value. Consistent with the normal accounting practice for a specific asset (eg as compared to a rate case for a large portfolio), the appropriate reimbursement should be the depreciated value of the original

installation cost. Notably, a RAB-derived value based on an arbitrary assignment of the average remaining life of the population may well exceed the initial installation cost for an aged asset, let alone a fairly depreciated value.

- The use of a RAB-derived value also presents an unreasonable barrier to exit from service provision by EnergyAustralia in the limited cases where it is feasible for Councils to remove EnergyAustralia lights and install their own lighting assets (eg in parks or CBD areas with underground supplied lighting).

### **ENERGYAUSTRALIA SUBMISSION SECTION 5: Maintenance Charges**

SSROC understands EnergyAustralia's proposed approach to regular billing for pre-2009 assets to involve splitting the charges into a fixed capital amount and separate maintenance charges and that this approach would be cost-neutral for Councils.

On this basis, SSROC has no objection to EnergyAustralia revising its billing approach as outlined with respect to capital and maintenance charges for pre-2009 assets.

SSROC however, strongly objects to the proposed basis for a fixed schedule of Residual Value charges for assets that are replaced early as outlined in comments on Section 4 above.

### ***Future Pricing Determinations***

As a vital public good but also a monopoly service that is not in the hands of those responsible for providing the service to the community, there should be absolute transparency of the costing models that public lighting pricing decisions are to be based on.

Inadequate disclosure has been a significant source of Council concern in this pricing review as outlined in the opening to this submission. This is particularly the case in the context of the large price increases sought by EnergyAustralia and the large differences in prices between utilities for substantially similar services often involving identical lights from the same manufacturer.

SSROC would strongly urge the AER to establish in its pricing Redetermination that, for future pricing reviews, all key financial and technical assumptions are publicly released and then validated and revised in an open process from the point of initial price proposals. This should include at a minimum:

- Component capital costs
- Assumed component lives, failure rates (supported by maintenance data) and asset replacement assumptions
- Consumables costs
- Labour costs
- Labour assumptions
- Assumed service standards and related maintenance assumptions
- Overhead rates
- A copy of the model in which these assumptions are input, preferably to a standard format

This approach would be consistent with recent Victorian ESC pricing reviews and consistent with the level of disclosure in the AER's February 2009 Energy Efficient Public Lighting Charges – Victoria Final Decision and the current on-going AER 2011-2015 Victorian pricing review.

SSROC welcomes further discussion with the AER about any of these items as well as matters raised in previously submitted documents.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'D. Lewis', with a stylized flourish at the end.

David Lewis  
General Manager  
Southern Sydney Regional Organisation of Councils