

25 October 2012

Economic Regulation of Network Service Providers Rule Change
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235



Attention Mr Richard Khoe

Dear Mr Khoe

ERC0134 - Consultation Paper on Savings and Transitional Arrangements

Energex Limited welcomes the opportunity to respond to the Consultation Paper on Savings and Transitional Arrangements to transition network service providers (NSPs) to the new Rules proposed in the Australian Energy Market Commission's (AEMC) draft rule determination.

In preparing this response, Energex has been in discussions with the Australian Energy Regulator (AER) and other NSPs and also participated in the AEMC's teleconference with industry members to further discuss alternative models. It is generally accepted that a 12 month delay to the upcoming round of resets is appropriate, and as such, the discussions have been primarily focussed on establishing revenue and prices for the intervening year with the aim of reducing price volatility.

Energex supports the principles highlighted in the Energy Network Association's submission in developing transitional arrangements. Taking the principles into consideration, the comments raised below reflect the outcome of discussions with the AER, AEMC and other NSPs in developing appropriate transitional arrangements.

Energex does not support the AEMC's proposal for a 'dual determination' process as this seems to represent an unnecessary use of resources, but rather believes that a single determination will result in a more streamlined and efficient transition to the new Rules. Energex supports the modified approach that results in the next regulatory determination being four years prospective and one year retrospective. In the event that prices for the first year need to be adjusted, this would be "trued up" in NPV neutral terms in the remaining years of the determination.

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Energex has considered the alternative models and has a preference for the proposed 'hybrid approach', as discussed at the teleconference of 23 October 2012 which provides that the placeholder revenue may be either:

- Below a cap specified in the Rules – in this case the proposal would automatically comply with the Rules and no public consultation would be required; or
- Above a cap specified in the Rules – in this case the AER would be required to conduct a more detailed assessment of the proposal using the approach set out in the TransGrid / AER proposal.

There would be a full review of revenue requirements for years 2-5 and the placeholder year in accordance with the new chapter 6 of the Rules and Guidelines. A true up mechanism would account for any difference between the placeholder revenue and the total revenue requirement for the full determination.

Revenue for Queensland NSPs in the placeholder year is to be based on information provided in a proposed pricing statement, which would be submitted as part of the regulatory proposal. Under this process the placeholder revenue is expected to move in the direction that will be consistent with the remaining years of the regulatory control period. The statement would be supported by relevant information for determination of the total revenue requirement.

Energex notes that the arrangement for capped revenue as envisaged by the AEMC (i.e. final year revenue with possible adjustment for CPI) is already provided under clause 6.11.3 and should be the deemed arrangement if a placeholder revenue cannot be settled in a timely manner. The 'hybrid approach' is much simpler and flexible; thereby reducing concerns about resourcing constraints and can accommodate NSPs varying revenue requirements.

In addition to the high level principles, Energex has raised additional matters that should be considered in the transitional arrangements while a full determination is being progressed. In discussions with the AER, there is general agreement that the following should apply as part of the transitional arrangements for the placeholder year:

- In relation to WACC, it is important for the transitional arrangements to adopt a pragmatic approach and provide certainty to the business; in particular on the cost of debt matters. It is proposed that the timing and length of the averaging period would be agreed between the AER and the NSP (subject to confidentiality requirements) as part of the framework and approach process;
- Distribution businesses would continue to have access to the same pass through events as they apply in the current regulatory control period;
- Service Target Performance Incentive Scheme (STPIS) targets and revenue at risk for the first year of the next regulatory control period would continue as applied in the last year of the previous regulatory control period;
- Any new capex incentive scheme would not apply in the first year of the next regulatory control period, but could apply in years 2-5 depending on the regulatory determination;
- In relation to the demand management and embedded generation connection initiative scheme (DMEGCIS) and efficiency benefits sharing scheme (EBSS), the transitional rules could deem a rollover from current arrangements to apply for the first year; and

- Unlike standard control services, there is no mechanism to “true up” any variations for alternative control services. As such, a number of options are under consideration, including CPI, continuing with the existing methodology or proposing new rates as part of the pricing proposal.

Further, Energex is seeking to specifically continue the operation of clause 11.16.10 (capital contribution policies) and clause 11.16.3 (treatment of regulatory asset base for shared assets) of the AER for the first year of its next regulatory control period.

In relation to process, and in consideration of the complexity and the transitional arrangements, Energex submits that the AEMC should provide opportunity for adequate consultation on the transitional arrangements, including publication of the draft rules prior to the making of a final determination. Should the AEMC have any questions in relation to this submission, please do not hesitate to contact Ms Rachel Leaver, Regulatory Determination - Regulation Manager on (07) 3664 4115.

Yours sincerely



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Strategy and Regulation