



Ref.: CP/JD

12 February 2010

Mr John Tamblyn
Chairman
Australian Energy Market Commission
Level 5, 201 Elizabeth Street
SYDNEY NSW 2000

97-99 Adelaide Street
Maryborough QLD 4650
PO Box 163
Maryborough QLD 4650
Telephone 13 10 46
Facsimile 07 4123 1124
Website www.ergon.com.au

www.aemc.gov.au ERC0097

Dear Mr Tamblyn

National Electricity Amendment (Payments under Feed-in Schemes and Climate Change Funds) Rule 2010

Ergon Energy Corporation Limited (Ergon Energy) appreciates the opportunity to comment on the Australian Energy Market Commission (AEMC) *Consultation Paper – National Electricity Amendment (Payments under Feed-in Schemes and Climate Change Funds) Rule 2010* (the Consultation Paper). Ergon Energy understands that the Consultation Paper released by the AEMC relates to the National Electricity Rules (the Rules) Change initiated by ETSA Utilities. This Rule change proposes changes to Chapter 6 of the Rules in relation to the payments made by Distribution Network Service Providers (DNSPs) under photovoltaic (PV) feed-in schemes and climate change funds established (or being established) by different jurisdictions. This submission is provided by Ergon Energy in its capacity as an electricity DNSP in Queensland.

By way of background, the Queensland Government introduced the Solar Bonus Scheme on 1 July 2008. The Solar Bonus Scheme is captured in section 44A of the Queensland *Electricity Act 1994* and requires distributors to pay eligible customers a feed-in tariff (FIT). The Queensland Government has not yet introduced a climate change fund.

Ergon Energy is generally supportive of the intent of the Rule Change proposed by ETSA Utilities. Ergon Energy believes that the Rule change is necessary in that an under-and-overs revenue adjustment for each regulatory year is more administratively simple to operate than the current approach proposed by the Australian Energy Regulator (AER) in its Draft Distribution Determination for Ergon Energy. It also allows for greater accuracy in forecasting payments under a FIT scheme, as the forecasts can be done annually as part of the Pricing Proposal process rather than for a five year period prior to the commencement of the regulatory control period.

Ergon Energy notes that any Rule change should not specify the way FIT and climate change funds should be recovered through network tariffs. Rather, it should be flexible enough to allow the various methodologies currently employed in various jurisdictions. That is, the Rule change should not require the recovery of FIT or climate change funds through individual specified components in the tariff and therefore the network bill i.e. currently in Queensland the only components identified within network tariffs are Distribution Use of System charges and Transmission Use of System charges. If the Rule change resulted in

distributors having to also separately identify FIT and climate change fund recovery in their tariffs, this would have significant system implications and well as increasing the administrative complexity of the arrangements for Ergon Energy.

Ergon Energy notes that the AEMC has asked stakeholders to provide comment on a number of specific issues as well as any other general aspects of the Rule change request. Ergon Energy provides specific responses to the issues for consultation raised by the AEMC below.

Administrative Requirements

- *How, and to what extent, does the current treatment for the recovery of payments under feed-in schemes and climate change funds under the Rules create an administrative burden for DNSPs and/or the AER?*
- *How, and to what extent, would the proposed Rule change amend the administrative processes for these types of costs, from the perspectives of DNSPs, the AER and other stakeholders?*

Ergon Energy understands that there is no provision in the Rules that provides for the recovery of payments made under governmental FIT schemes and climate change funds. Currently in Queensland, while the Queensland Government stated that the costs of the scheme would be recovered from all customers, the Queensland Competition Authority has not allowed Ergon Energy to recover these costs from customers. As a consequence, in its Regulatory Proposal, Ergon Energy has proposed that commencing 1 July 2010 an annual unders and overs revenue adjustment operate to enable the collection of funds associated with payments to customers with eligible PV systems. Ergon Energy sought to have adjustments for the FIT as a feature of the control mechanism, rather than as a pass through event.

Ergon Energy believes that if an annual unders and overs revenue adjustment is provided for in the Rules, this will reduce the administrative processes and costs associated with operating the scheme. Ergon Energy considers that the proposed process will provide several key benefits for customers, DNSPs and AER, in that it will:

- provide for more accuracy for customers in terms of pricing;
- offer a simplified application process for DNSPs;
- reduce compliance costs for DNSPs by removing the need to generate and substantiate forecasts as part of the Distribution Determination and costs pass through process; and
- reduce compliance assessment costs for the AER by removing the need to obtain validation of forecast methods and estimates prepared by DNSPs.

Ergon Energy considers that the proposed Rule change will reduce the current proposed administrative burden. The current Rule change proposed by ETSA Utilities to have FITs treated as a annual revenue adjustment is largely consistent with what Ergon Energy proposed in its June 2009 Regulatory Proposal. Ergon Energy believes that the FIT event should be treated as an unders-and-overs feature of the revenue Control Mechanism.

Allocation of Risks and Customer Impact

For the purposes of modelling its Revised Regulatory Proposal, Ergon Energy prepared a forecast of payments under the Queensland FIT scheme as a component of operating expenditure. However, as set out in ETSA Utilities' request for a Rule change, forecasting

FIT payments is highly uncertain as they are based on projections of the behaviour of others over which DNSPs have no control. Ergon Energy believes that providing a five year forecast as part of a Distribution Determination process results in significant uncertainty for DNSPs and customers. Recovering the cost of the scheme through the annual unders and overs process reduces the uncertainty and therefore the risk to all parties.

- *What factors are taken into account by DNSPs in preparing forecasts of payments under feed-in schemes and climate change funds as a component of operating expenditure?*

In preparing the forecasts of FIT payments for its Revised Regulatory Proposal, Ergon Energy used 12 months of historical actual data to develop an historical trend. This was then used to forecast out payments for the rest of the financial year 2009-10. The same historical trends were applied to calculate the forecast for the 2010-11 FIT forecast. For the remaining years of the next regulatory control period, Ergon Energy applied the forecast growth rates that were applied by ETSA Utilities in their Regulatory Proposal¹. These rates have been reviewed by Australian Energy Market Operator (AEMO) on request from the AER. Ergon Energy understands that the AER has accepted ETSA Utilities growth forecasts.

Ergon Energy took this approach because it is highly likely that PV uptake will continue to increase in the future. However, because the uptake depends on a range of external factors over which Ergon Energy has no control and there is little publicly available information on some of these factors, the future growth rates are unknown and highly uncertain. Therefore it was considered that the most conservative approach was to rely on known historical data and publicly available forecasts that have been reviewed by independent parties.

While Ergon Energy has taken a conservative approach in preparing its Revised Regulatory Proposal, we still consider that that the forecasts of FIT payments are highly uncertain and consequently should not form part of the AER's Final Distribution Determination. Rather, the FIT should be accounted for through an annual revenue adjustment at the end of each regulatory year which will provide more certainty for customers.

- *What considerations or safeguards may be taken into account by DNSPs to minimise any errors in the forecast values? That is, what actions are taken by DNSPs to minimise any potential risks from forecasting errors?*

By using historical data and relying on AEMO's assessment of ETSA Utilities' Sales and Demand Forecasts², Ergon Energy has taken a conservative approach to its forecasting of FIT payments. However, Ergon Energy submits that in order to minimise potential risks from forecasting errors, the AEMC should consider a Rule amendment that provides for an under-and-overs annual revenue adjustments rather than relying on the cost pass through process. Ergon Energy considers that this will:

- reduce compliance costs for DNSPs by removing the need to generate and substantiate forecasts as part of the Distribution Determination process

1

<http://www.aer.gov.au/content/item.phtml?itemId=732136&nodeId=e05cbe25f52fd424a9aa478303617c29&fn=AEMO%20report.pdf>

2

<http://www.aer.gov.au/content/item.phtml?itemId=732136&nodeId=e05cbe25f52fd424a9aa478303617c29&fn=AEMO%20report.pdf>

- reduce administrative costs for DNSPs by removing the need to prepare cost pass through applications; and
 - reduce compliance assessment costs for the AER by removing the need to obtain validation of forecast methods and estimates prepared by DNSPs and assessing cost pass through applications.
- *Where the actual operating expenditure differs from the forecast values, what actions would DNSPs take? That is, how would the nominated pass-through provisions function in practice and how is the recovery of payments affected year-on-year?*

As the AER's Distribution Determination does not commence until 1 July 2010, Ergon Energy has not been required to apply the pass through provisions to date. Therefore, the process remains uncertain. Ergon Energy's understanding is that the nominated pass through event provisions would operate once Ergon Energy receives confirmation from the AER that its audited regulatory accounts have been accepted. If the difference between actual and forecast expenditure met the threshold set by AER in the Final Distribution Determination (not known until 30 April 2010) then Ergon Energy would need to prepare and submit a pass through application to the AER. As the AER has not prepared any guidelines on the cost pass through process, it is not yet known what level of detail and justification Ergon Energy will be required to provide as part of this process. Any adjustments to the Annual Revenue Requirement (ARR) would take effect two years after the year in which the actual results differ from forecast i.e. if the variance occurs in 2010-11, and then the ARR (and network tariffs) will not be adjusted until 2012-13. It should be noted that the recovery of payments under a pass through mechanism will depend on the AER's Maximum Allowable Revenue (MAR) formula which will be set by the AER in their Final Distribution Determination. The AER in the Draft Distribution Determination (released on Nov 2009) indicated that in order to account for cost pass throughs, a term 'passthrough' has been included in the MAR and side constraint formulas set out in the AER conclusion section.

Savings and transitional requirements

- *What factors should be taken into account in developing savings and transitional provisions to enable efficient potential application to all DNSPs recognising that each DNSP is at a different point in the regulatory cycle?*

The AER is expected to release the Final Distribution Determinations for three DNSPs, Ergon Energy, ENERGEX and ETSA Utilities by 30 April 2010. Ergon Energy notes that the AEMC have indicated in the Consultation Paper *"that the timetable for the Rule change process under the NEL, it is unlikely that the Rule change will be completed prior to the AER making its final revenue determination for ETSA Utilities"*³. Therefore transitional arrangements will be required to support all three DNSPs.

Ergon Energy supports the AEMC having due regard of the impact a Rule change will have on Ergon Energy's Distribution Determination when contemplating this proposed amendment to the Rules. Ergon Energy considers that the AEMC should ensure that there is a transitional arrangement whereby Ergon Energy can immediately apply the Rule, therefore requiring an amendment to Ergon Energy's Distribution Determination. However, this is subject to Ergon Energy's earlier concern that the Rule change not specify the way FIT and climate change funds should be recovered through network tariffs. If Ergon Energy is required to separately identify FIT and climate change fund recovery in its tariffs, this would

³ p7, the Consultation Paper

have significant system implications and well as increasing the administrative complexity of the arrangements for Ergon Energy.

Jurisdictional requirements

The proposed Rule would potentially apply to FIT schemes and climate change funds that are yet to come into effect.

- *Should the Rules include a set of criteria that a scheme would need to meet in order to use the proposed cost recovery mechanism? If so, what should be included in the criteria?*

Ergon Energy considers it appropriate that given that FIT Schemes and Climate Change Funds are essentially mandated by state governments, and it is likely that new schemes may be introduced in the future (or existing schemes expanded) it would be appropriate for the Rules to include a set of criteria that a scheme would need to meet in order to use the cost recovery mechanism. Ergon Energy believes that the criteria specify that the scheme or fund:

- is mandated by the Government (State or Federal); and
- includes a regulatory requirement on the DNSP to make the payment.

Ergon Energy would be pleased to discuss this submission with the AEMC.

Yours sincerely



Carmel Price
Group Manager Regulatory Affairs

Telephone: 07 41219545
Facsimile: 07 3228 8130
Email: carmel.price@ergon.com.au

c.c.: Jenny Doyle, Manager Regulatory Affairs – Network Regulation