

ELECTRICITY TRANSMISSION NETWORK owners

Draft National Electricity Amendment (Pricing of Prescribed Transmission Services) Rule 2006

Supplementary Submission in Response to AEMC Draft
Rule Determination

12 December 2006



Cost allocation

ETNOF appreciated the opportunity to meet with Commissioner Carver and AEMC staff on 6 December 2006, to clarify a number of issues of interpretation regarding the draft Pricing Rule, and the cost allocation process set out in clauses 6A.24.2 and 6A.24.3.

With respect to clause 6A.24.2, ETNOF understands that the Commission's intention is that the cost allocation process can be done expeditiously and that neither a high degree of precision nor fine judgement calls are required. ETNOF supports that approach and, indeed, would be concerned if its members were required to undertake a major cost reallocation task that would require considerable resources and time.

Subsequent to our meeting on 6 December, ETNOF identified a further issue in relation to the intended operation of clause 6A.24.2 which ETNOF would like to bring to the Commission's attention. The issue is whether the concept of "directly attributable (on a causation basis)" applies:

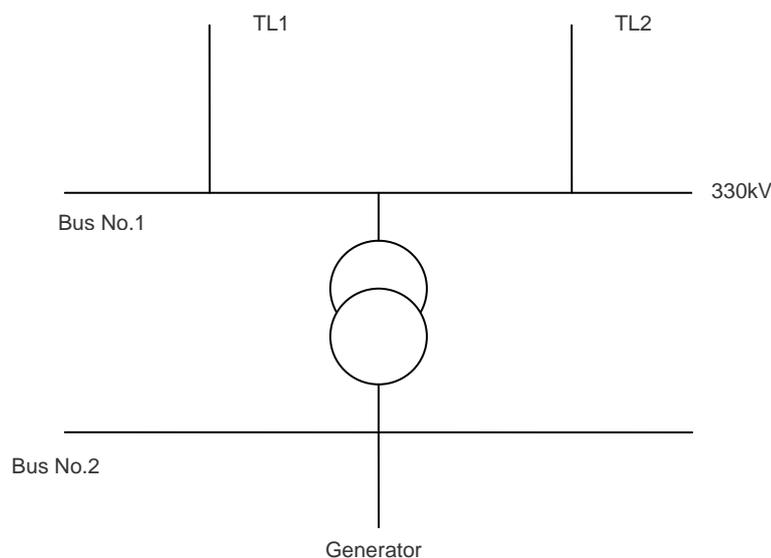
- at an aggregated level (at the level of substations and transmission lines) (**Approach 1**); or
- whether it applies at a more granular level (such as circuit breaker bays and substation establishment costs) (**Approach 2**).

ETNOF believes that the choice of approach could have a material impact on the resulting cost allocation, and therefore in ETNOF's view it is essential that the Pricing Rule mandates a particular approach.

The remainder of this submission explains this issue in more detail using an illustrative example, and explains ETNOF's preferred interpretation of the draft Pricing Rule.

What ETNOF understands is required (Approach 1)

For illustrative purposes, consider the following diagram of a simple sub-station connecting the shared network to a generator. Note that this example is a simplified illustrative example and the principles established would in fact require considerable work once applied to more complicated actual systems.



In the past ETNOF members have typically undertaken cost allocation with this level of granularity. Modifying the existing cost allocation process to comply with the new draft rule would involve:

- (a) allocating the costs of the transmission lines TL1 and TL2 which form part of the transmission network to TUOS;
- (b) allocating the costs of the transformer and generator connection (including circuits breakers, protection etc) to connection charges;
- (c) the costs of the land, building, fences and other assets not directly attributable to TUOS or connection assets would be allocated using the priority ordering in Clause 6A.24.2(d). The effect of this priority ordering would be to allocate these shared costs to TUOS.

Importantly, there are very considerable costs in (c) and consequently, a preliminary conceptual application of the above process to one ETNOF member's system shows that:

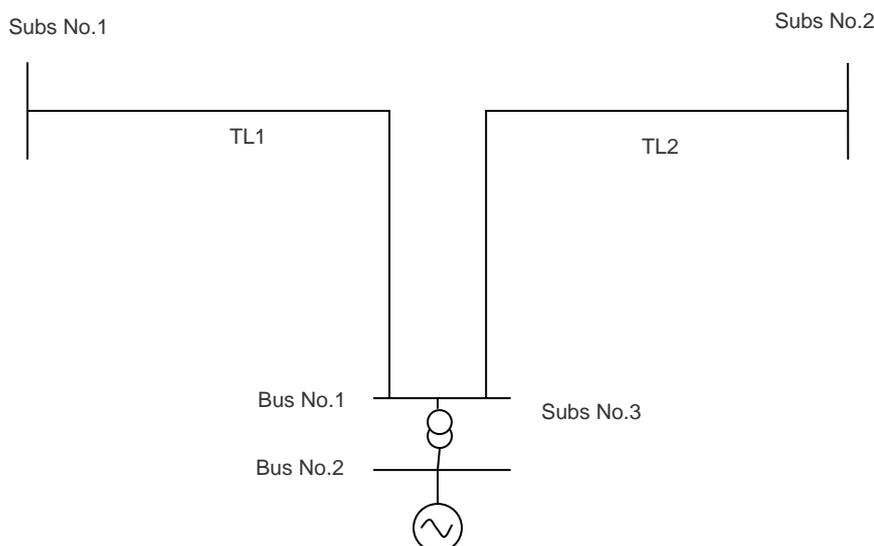
- generators would see a significant reduction in charges; and
- customers would see an increase in charges and, depending upon the customer, this could range up to approximately a 10% increase for a direct connect customer.

As an aside, it is also noted that draft Rule 6A.24.2(d) supposes that allocating costs on a "directly attributable" basis would lead to item (c) to be over-allocated. This is because the assets in question are required to provide connection services and use of system services. However, contrary to the drafting of Rule 6A.24.2(d), if assets are jointly required to provide two categories of service it would be reasonable to conclude that the assets in question **cannot** be 'directly attributable (on a causation basis)' to any particular service category. On this view, the priority ordering would be required to address a pool of costs that cannot be directly allocated in the first instance, whereas the draft Rule uses the priority ordering to address an over-allocation of costs. It may be useful for the Commission to clarify this issue in its Rule Determination.

What ETNOF understands is not required (Approach 2)

Conceptually, the cost allocation process in the draft Pricing Rule could be applied at a much higher level of granularity.

Consider the following diagram which in fact is the same as that above but shows how the hypothetical substation is connected into the system as a whole. Again it is important to note that this diagram is also a simplification compared with any ETNOF members' systems.

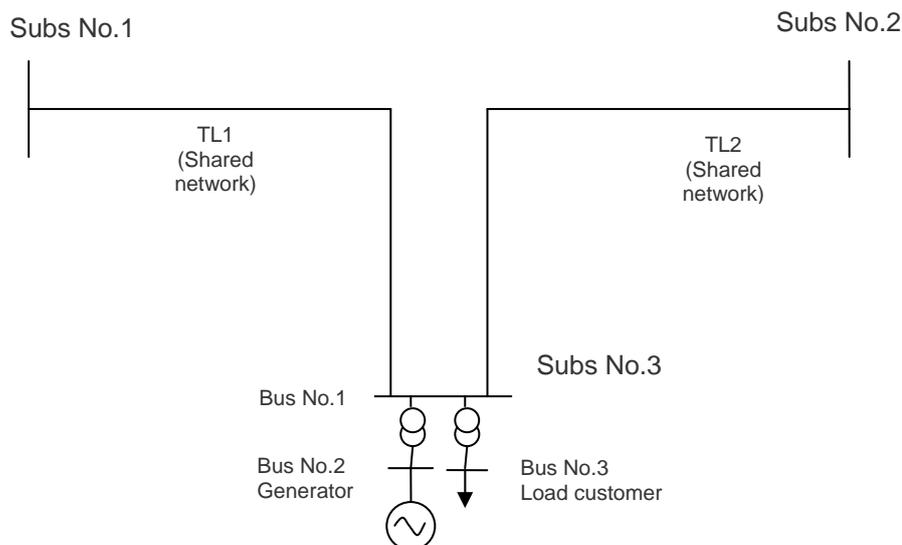


By taking a much broader perspective to the question of causation, in the above example it is possible to regard the whole of the substation as solely servicing the generator because it would be possible to build a transmission line directly from substation 1 to 2 without substation 3 existing at all.

The consequences would likely include:

- if this approach were adopted it would shift a great deal of costs in the reverse direction. Load customers would see a reduction in costs and generators and some direct connection customers may see a significant increase in costs. This result occurs because substation 3 can be considered to be “directly attributable (on a causation basis)” to the generator. The more granular consideration of shared costs within the Substation No.3 that applied in the previous example would no longer be applicable.
- the cost allocation exercise would be very different from any previous cost allocation process undertaken by members; and
- the cost allocation exercise would in many instances likely become a deeply philosophical exercise of considering what the system might look like in the absence of certain users. Indeed, at one level the system would not exist at all without both generators and customers so depending on how the hypothetical deconstruction was undertaken, and in particular the order of the deconstruction, there could be vast swings of costs between users.

Furthermore, this approach may lead to some significant inequitable outcomes as described in the next example.



In this situation the substation services both a generator and a customer load. As before, the substation establishment cost is a cost that is allocated using the priority ordering approach of Clause 6A.24.2. However, in this case this cost will be allocated to TUOS, since in the absence of the generator the substation is still required to service the customer load. This is an inequitable treatment of these costs compared to the previous example.

These examples illustrate that this type of allocation process is likely to be unacceptably resource intensive for ETNOF members and may prove to be highly contentious and unpredictable for users.

ETNOF would appreciate the opportunity to discuss the Commission’s views on the issue raised in this submission, and to follow-up on the matters of interpretation that were discussed on the 6 December. As noted previously, ETNOF welcomes the opportunity to work more closely with the Commission as it finalises the Pricing Rule.