



Trans Tasman Energy Group

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7 December 2012

**Australian Energy Market Commission
Level 5, 201 Elizabeth Street
Sydney NSW 2000**

Re: Proposed Rule Change

Trans Tasman Energy Group (TTEG) requests that the Australian Energy Market Commission (AEMC) consider making the enclosed proposed Rule changes under section 91(1) of the National Electricity Law.

In making this request we are:

- Retracting the rule change requests submitted on 15 October 2012 (original) and on 1 December 2012 (revised); and
- Submitting a revised rule change request to include all the matters raised and refer to the date of the revised request which includes the information set out below.

The proposed Rule changes would require that the:

1. Cost Allocation Method (CAM, NER 6.15.4):
 - is included in the distribution consultation procedures (NER 6.16), and
 - contains values against the cost allocators to enable effective price negotiation, and that the
2. price for a *negotiated distribution service* must be based on the costs incurred in providing that service.

We would welcome the opportunity to provide any further input required by the AEMC to assess our request.

Yours sincerely,

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PROPOSED RULE CHANGES

1 Introduction

Trans Tasman Energy Group (TTEG) is an energy sector consultancy specialized in providing commercial and regulatory advice to our clients throughout the NEM.

In its role of assisting our clients, we have been actively involved in attempting to establish services and prices under NER Ch 6 Part D – Negotiated Distribution Services.

In this regard, TTEG has firsthand experience in the issues for which we are proposing the Rule changes.

2 Description of the proposed Rules

The proposed Rule changes would require the AER to undertake the NER's *distribution consultation procedures* (NER Ch 6 Part G), to amend or replace the *Distribution Network Service Provider's Cost Allocation Method*."

To provide a quantitative indication to users of a DNSP' *Cost Allocation Method* (CAM), we also propose that values (eg dollars, percentage, or some other meaningful measure) be allocated to components in a DNSP's CAM to provide visibility pertaining to a DNSP's costs to customers (Service Applicants) in establishing prices for Negotiated Distribution services under NER Ch 6 Part D.

Finally, to provide a clear direction as to how Negotiated Distribution service prices are to be established, we propose that the price for a *negotiated distribution service* must be based on the costs incurred by the *Distribution Network Service Provider*.

3 Issues in relation to the current Rules

Cost Allocation Method

The DNSP's CAM is included in the Negotiation Process (including NER 6.7.1) and as such should be open to review so customers can assess the appropriateness of the distributor's CAM for this process, which includes establishing prices for Negotiated Distribution services.

We note NER 6.16 requires consultation where the AER is developing or amending any guidelines, models or schemes, or in reviewing any values or methods - yet the CAM (a "method") has not been identified in NER 6.15 as requiring such a consultation.

Pursuant to NER 6.7.2, when the provider is negotiating the *terms and conditions of access* to *negotiated distribution services*, a *Distribution Network Service Provider* must comply with:

- (1) *the provider's negotiating framework; and*
- (2) *the provider's Negotiated Distribution Service Criteria.*



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Further, the *Distribution Network Service Provider* should establish costs for *negotiated distribution services* pursuant to the principles in NER 6.7.1, which are ultimately included as Negotiated Distribution Service Criteria (NDSC) in the *Distribution Network Service Provider's negotiating framework*.

6.7.1 Principles relating to access to negotiated distribution services

The following principles constitute the *Negotiated Distribution Service Principles*:

- (1) the price for a *negotiated distribution service* should be based on the costs incurred in providing that service, determined in accordance with the principles and policies set out in the *Cost Allocation Method* for the relevant *Distribution Network Service Provider*;

It follows that the *Cost Allocation Method* is a primary input to establishing prices for *negotiated distribution services* and for customers assessing the *Distribution Network Service Provider's* offer pursuant to the *negotiating framework* including items under NER 6.7.5:

- (c) The *negotiating framework* for a *Distribution Network Service Provider* must specify:
 - (1) a requirement for the provider and a *Service Applicant* to negotiate in good faith the *terms and conditions of access* to a *negotiated distribution service*; and
 - (2) a requirement for the provider to provide all such commercial information a *Service Applicant* may reasonably require to enable that applicant to engage in effective negotiation with the provider for the provision of the *negotiated distribution service*, including the cost information described in subparagraph (3); and
 - (3) a requirement for the provider:
 - (i) to identify and inform a *Service Applicant* of the reasonable costs and/or the increase or decrease in costs (as appropriate) of providing the *negotiated distribution service*; and
 - (ii) to demonstrate to a *Service Applicant* that the charges for providing the *negotiated distribution service* reflect those costs and/or the cost increment or decrement (as appropriate); and
 - (iii) to have appropriate arrangements for assessment and review of the charges and the basis on which they are made; and
 - (4) a requirement for a *Service Applicant* to provide all commercial information the provider may reasonably require to enable the provider to engage in effective negotiation with that applicant for the provision of the *negotiated distribution service*;

Pursuant to NER 6.15 a *Distribution Network Service Provider* must comply with the *Cost Allocation Method* that has been approved in respect of that provider from time to time by the AER.



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Pursuant to NER 6.15.4 (b) the *Cost Allocation Method* proposed by a *Distribution Network Service Provider* must give effect to and be consistent with the *Cost Allocation Guidelines*.

Whilst the *AER* may, from time to time, and in accordance with the *distribution consultation procedures*, amend or replace the *Cost Allocation Guidelines (NER 6.15.3 (d))*, there is currently no requirement for the *Cost Allocation Method* to be subjected to the *distribution consultation procedures*.

Regarding allocation, NER 6.15.2(4) provides "any cost allocation method which is used, the reasons for using that method and the numeric quantity (if any) of the chosen allocator must be clearly described;"

Further, current *Cost Allocation Methods* do not contain sufficient information (allocators) to enable:

- customers to engage in effective negotiation with the provider regarding the price for the provision of the *negotiated distribution service*, (NER 6.7.5(c)(2)), and
- the DNSP "to identify and inform a *Service Applicant* of the reasonable costs and/or the increase or decrease in costs (as appropriate) of providing the *negotiated distribution service*;" (NER 6.7.5(c)(3)(i))

The fundamental issue is that without any values (eg dollars, percentage, or some other meaningful measure) allocated to components in a DNSP's *Cost Allocation Method* customers are not able to effectively establish if the *Distribution Network Service Provider's negotiated distribution service* price offer is NER compliant, including whether the same cost was allocated more than once (NER 6.15.2(5))

NOTE: A change to the *Cost Allocation Guidelines* may also be required to ensure "the detailed information that is to be included in a *Cost Allocation Method*" (NER 6.15.3 (c)(2)) can be effectively met.

Re 6.7.1(1)

"6.7.1(1) the price for a *negotiated distribution service* should be based on the costs incurred in providing that service, determined in accordance with the principles and policies set out in the *Cost Allocation Method* for the relevant *Distribution Network Service Provider*;" (our underline)

We propose that "the price for a *negotiated distribution service* must be based on the costs incurred....."

Whilst we accept and understand the negotiating parties may (in theory) agree any method to establish prices, as a significant imbalance of market power exists between the negotiating parties, requiring prices to be based on the cost incurred provides a "default" position on how prices must be established.

Further, should the negotiation be referred to the AER for resolution, the AER has clarity in direction as to how to determine prices.



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4 Impact on Others

The impact of the proposed Rule change pertaining to the *Cost Allocation Method (CAM)* is that all *Distribution Network Service Providers (DNSPs)* would be required to include sufficient information in their CAM such that customers would be able to effectively establish the DNSP's costs for providing the Negotiated Distribution Service pursuant to NER 6.7.1(1).

Further, by including appropriate information, the DNSPs will be able to more easily provide information pursuant to NER 6.7.5(c)(3)(i) and to demonstrate compliance pursuant to NER 6.7.5(c)(3)(ii).

Customers seeking to negotiate a service (pursuant to NER Ch 6 Part D) will have additional information (as required by NER 6.7.5(c)(2)) to establish if the *Distribution Network Service Provider's negotiated distribution service* price offer is NER compliant, including whether "the same cost must not be allocated more than once" (NER 6.15.2(5)), something which customers currently cannot do.

The benefit through the provision of additional information will also flow to the AER, if the AER is required to resolve a dispute under the *Distribution Network Service Provider's Negotiating Framework*.

5 Description of the proposed solution for each issue

The proposed solution is to require *Distribution Network Service Provider's* to include values (either dollars, percentage, or some other meaningful measure) allocated to Negotiate Distribution Service components in their *Cost Allocation Method* so that customers have visibility to the costs incurred by the DNSP in providing a service that is being negotiated.(NER 6.7.1)

South Australian Power Network's CAM already contains some such information as shown in the following table from page 25 of its CAM.

In consideration of the CAM's contribution in establishing negotiated distribution prices (NER 6.7.1(1)), we propose the *AER* be required to undertake the *NER's distribution consultation procedures* for any changes to a *DNSP's Cost Allocation Method (CAM)*.



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Finance Department (excluding CFO)	Causal Allocator	Standard Control		Negotiated Distribution		Unregulated		Total \$'000
		\$'000	%	\$'000	%	\$'000	%	
Corporate Finance	Total Revenue	1,265	72%	171	10%	320	18%	1,756
Operational Finance - DaNM, Field Services, Services	Regulated Revenue, CaMS to Unregulated	689	88%	93	12%	0	0%	782
Operational Finance - CaMS	Unregulated	0	0%	0	0%	565	100%	565
Regulatory Finance	Regulated Revenue	389	88%	53	12%	0	0%	441
Accounts Payable	Creditor Transaction Volumes	238	79%	18	6%	45	15%	301
Payroll	FTE Splits	207	81%	18	7%	31	12%	256
Purchasing and Contracts	Stock Material & Service Contract costs	811	71%	113	10%	219	19%	1,143
Directly Attributed*	Standard Control only	516	100%	0	0%	0	0%	516
Total Finance (excl CFO)		4,114	71%	465	8%	1,179	20%	5,759
CFO Costs	Weighted Average of Finance Allocators	311	71%	35	8%	89	20%	435
Total Finance (incl CFO)		4,425	71%	500	8%	1,268	20%	6,194
* includes accounts receivable for asset damage and taxation consulting costs, directly attributed to standard control services as a cost of operating the electricity distribution network.								

Our proposed solution for NER 6.7.1(1) is that the price for a Negotiated Distribution Service must (and not "should") be based on the cost incurred in providing that service.

NOTE: The AER has already recognised the benefit of this approach by including the following in Appendix C (Negotiated distribution service criteria) in its 2010-11 to 2014-15 South Australian Distribution Determination as follows:

"5. The price for a negotiated distribution service must reflect the costs that a DNSP has incurred or incurs in providing that service, and must be determined in accordance with the principles and policies set out in the DNSP's Cost Allocation Method." (our underline)

6 Costs and Benefits

The cost to undertake the *distribution consultation procedures* for the CAM would be the cost incurred by the AER in conducting its *distribution consultation procedures (NER Ch 6 Part G) for the Cost Allocation Method*.

We do not expect any significant cost to be incurred by DNSPs as they will have already established costs for components in preparing their *regulatory proposal*.

The expected benefits resulting from the Rule changes are:

- customers will have information to enable effective negotiation of the price for services under NER 6.7.1(1)



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- customers will have additional information (NER 6.7.5(c)(2)) to establish if the *Distribution Network Service Provider's negotiated distribution service* price offer is NER compliant, including whether the same cost was allocated more than once. (NER 6.15.2(5)), and
- customers, DNSP and the AER (if required to resolve a dispute) will have better cost information and process to establish NER compliant prices.

We are not aware of the current market value of negotiated distribution services, but we reasonably expect it will increase over coming years through the increased classification of services as negotiated services. An example is public lighting which is already classified as a *negotiated distribution service* in SA, with various (increasing) aspects of public lighting services classified as negotiated in other jurisdictions.

7 Contribution of proposed Rule change to the National Electricity Objective

The proposed Rule changes will contribute to the achievement of the National Electricity Objective and the long term interests of consumers requiring negotiated distribution services, as they will enable:

- Negotiated Services to be established by customers on a "cost reflective" basis, and
- Efficient investment (by the DNSP) in these services as the "best value" outcome can be negotiated by the customer to meet their individual needs in terms of price, quality, safety, reliability and security, while at the same time ensuring that the DNSP's efficient costs are recovered.

8 Draft of proposed Rule

NER 6.15.4 to include a new clause:

"The *AER* may, from time to time and in accordance with the *distribution consultation procedures*, amend or replace the *Distribution Network Service Provider's Cost Allocation Method*."

NOTE: Other clauses in 6.15.4 will require to be adjusted to reflect this requirement.

NER 6.15.2(4) to be revised.

"(4) any cost allocation method which is used, the reasons for using that method and the numeric quantity ~~(if any)~~ of the chosen allocator must be clearly described;

NER 6.7.1(1) to be revised to:

"the price for a *negotiated distribution service* must be based on the costs incurred in providing that service, determined in accordance with the principles and policies set out in the *Cost Allocation Method* for the relevant *Distribution Network Service Provider*,"

END