



Cost pass through amendments

Final rule determination – 2 August 2012

The AEMC today published its final rule determination on amendments to the National Electricity Rules relating to the cost pass through provisions that apply to transmission and distribution network service providers.

Cost pass through amendments to the National Electricity Rules (NER) Proposed amendments – Grid Australia’s rule change request

Grid Australia submitted that under the NER, transmission and distribution businesses are exposed to the risk of significant costs arising from natural disasters and insurance liability limits that are outside of their reasonable control. To address those risks, Grid Australia proposed amendments to the NER. The details of those amendments may be found in Grid Australia’s rule change request on the AEMC’s homepage.

Overview of the AEMC’s final rule

The AEMC has determined to make a more preferable final rule. Minor drafting amendments identified by stakeholders during consultation on the draft rule determination have been incorporated in the final rule.

The AEMC’s policy position remains that cost pass throughs should be only used where other, more suitable means of addressing these costs are less appropriate.

The aim of these amendments is to enable network businesses to recover their efficient costs in the advent of an unexpected event, while ensuring that the prices for consumers are no more than necessary to provide an appropriate level of service.

To achieve this, the AEMC has determined to:

- provide transmission businesses with the ability to nominate additional pass through events as part of their revenue proposals;
- include a set of ‘nominated cost pass through event considerations’ in the NER that the Australian Energy Regulator (AER) must consider when deciding whether to accept the transmission or distribution business’ proposed pass through event;
- remove the terrorism event from the prescribed pass through events under the NER for both transmission and distribution businesses; and
- provide transitional arrangements for network businesses who have recently completed or are in the middle of their revenue determination with the AER.

The AEMC has also agreed to the inclusion of amendments to address the ‘dead zone’, a known anomaly in the drafting in the NER relating to the timing of a cost pass through for both transmission and distribution businesses.

Resultant categories of pass through event

As a result of the AEMC’s final rule, the prescribed pass through events for each type of network business will be as follows.

Distribution network service providers

- a regulatory change event;
- a service standard event;
- a tax change event;
- a retailer insolvency event; and
- in addition to those above, a nominated event for a regulatory control period.

The Commission has made a rule that enables transmission network service providers to nominate additional pass through events as part of their revenue proposals, subject to the nominated pass through event considerations in the rules.

The final rule also addresses the 'dead zone' anomaly for all network service providers.

Transmission network service providers

- a regulatory change event;
- a service standard event;
- a tax change event;
- an insurance event; and
- in addition to those above, a nominated event for a regulatory control period.

Transmission businesses also have the ability to utilise the capital expenditure re-opening and contingent event mechanisms under the NER.

Addressing unexpected events – role of cost pass through

The forecast efficient expenditure of network service providers in Australia is regulated by the AER and recovered through their allowed revenue, set each year. This allowed revenue includes the cost of risk management mechanisms, including commercial and self-insurance.

Currently there are two ways that a network business may recover the costs incurred as the result of any significant events that were not forecast as part of their allowed revenues. Namely:

1. Cost pass through – where expenditure arises in a permitted category of event (prescribed or nominated), the network service provider may apply to the AER to recover this amount from electricity customers in the next year's prices.
 - Prior to this rule, distribution network service providers were able to propose additional categories of pass through events (at the time of their AER revenue determination). For example, in the AER's 2010 review of Victorian Electricity Distribution Price Review for 2011-2015, the distribution network providers proposed a natural disaster cost pass through category. The AER reviewed the proposal by the networks and included this category as part of its determination.
 - Unlike distribution networks, transmission networks were not able to propose additional categories of pass through events, as the national electricity rules did not extend this ability to them.
 - A cost pass through event nominated at the time of a network determination and approved by the AER only covers that category of event for that regulatory control period.
2. Capital expenditure re-opener - transmission network service providers can currently propose a capital expenditure re-opener to the AER. This only covers capital expenditure (e.g. the replacement cost of assets poles and wires swept away by flooding). It does not enable the recovery of repair costs to any assets which are damaged, but not destroyed. The capital expenditure re-opener is currently not available to distribution businesses, but is being considered by the AEMC in the economic regulation of electricity networks rule change request submitted by the AER.

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