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19 January 2009

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

By email to submissions@aemc.gov.au

Dear Dr. Tamblyn,

RE: Supplementary Submission to Victorian Derogation – Advanced Metering Infrastructure Rollout, Draft Rule Determination

AGL Energy Limited (**AGL**) is concerned that the amendments of the Victorian Cost Recovery Order in Council¹ (**Revised Order**) could have a material impact on the efficient cost and transition to contestability in the provision of AMI services. This submission is in addition to one dated 07 November 2008 (**First Submission**) and is in response to the Revised Order.

The Commission had considered the derogation determination on the basis that a cost recovery approach was provided in an original Order in Council² (**Original Order**) that was consistent with the revenue and pricing principles in the National Electricity Law³. The cost recovery approach in the Original Order is based on the well established "CPI-X" price control regime that provides for an incentive mechanism to reveal and achieve efficient cost and share any efficiency gain derived from the AMI rollout with the customers.

This form of regulation in the Original Order was, however, changed significantly on 25 November 2008. The Revised Order is now based on a cost pass through arrangement that apparently provides limited scope for Australian Energy Regulator (**AER**) to enforce a cost efficiency regime and a transparent accounting of efficiency gain that can be passed through to the customers.

AGL is concerned that the amended approach does not provide control and oversight on the efficient cost of implementing AMI in Victoria. In AGL's view, it is prudent that the final determination of the derogation should contain appropriate regulatory requirements for achieving an efficient rollout to ensure that a net saving can be achieved.

¹ Victorian Government Gazette, 25 November 2008, No. S314.

² Victorian Government Gazette, 28 August 2007, No S200

³ Section 3.4.3, Draft Rule Determination, AEMC, 25 September 2008

AGL remains of the belief that a market approach would provide and sustain a downward pressure on the cost of introducing AMI in the long run⁴. In our First Submission, AGL suggested that this could be achieved by preserving the current Chapter 7 provision for customer choice of Type 4 meters. The flexibility for customers and retailers to choose an alternative metering solution provides an effective market-based test on the assumption that efficient cost can best be achieved by a distributor-led mass rollout of AMI meters. In another submission, AGL also highlighted that we did not believe that the assumption on cost efficiency, which was one of the key determinants for the decision on a DB-led rollout, was sufficiently validated in the industry cost-benefit analysis as the impact of competition on the cost of rollout had not been adequately considered⁵. This untested cost efficiency assumption and a potential lack of regulatory oversight makes it critical that an effective form of checks and balances should be provided. This would ensure that the expected rollout efficiency can be realised, and thereby, the potential to achieve the National Electricity Objective on efficient investment would not be compromised.

In our First Submission, AGL welcomed the Commission and MCE's commitment to ensure that a transition to a contestable market in metering services would be considered in the regulatory arrangement for the AMI rollout. AGL also expressed its support for the Commission's suggestion to provide regulatory measures that would facilitate this transition. In AGL's view, the new cost recovery approach of the Revised Order further highlights the importance of having such a transition and the Commission's role in facilitating it. The transition, however, will be hard or require an extended period to achieve an effective transition if the switching cost barrier is high and in particular, if there is a lack of a consistent operating platform across all jurisdictions and distribution areas, which was another concern that AGL raised in the First Submission.

It is also not evident in the Revised Order that measures are provided to minimise barriers to the transition to competition in the post-derogation period. For example, an accelerated depreciation that could reduce the undue delays in the transition, as suggested in the Commission's Draft Rule Determination, was not evident in the revised order. Similarly, other measures such as a detailed disclosure of cost structure and breakdowns of AMI infrastructure are also not apparent in the Revised Order. AGL is concerned that the transition to contestability of metering service can be adversely hampered by the lack of appropriate regulatory requirements in the Revised Order.

In summary, AGL believes that the Commission should provide a range of conditions in its final approval of the derogation to improve regulatory oversight on the rollout of AMI in Victoria, namely:

- A framework to ensure that rollout cost is efficient and efficiency gains are passed through to the customers promptly;
- Regulatory measures are provided to minimise barriers for the transition to contestability of metering services including an open access arrangement; and
- A provision that requires a review on the effectiveness of these conditions during the derogation period.

⁴ AGL submission to MCE Cost Benefit Analysis of Smart Metering and Direct Load Control, 16 April 2008

⁵ AGL submission to Regulatory Impact Statement of Phase 2 that accompanies MCE's consideration on Smart Meter Rollout, 16 May 2008



AGL is aware that the Commission intends to provide a final determination of the derogation on 29 January 2009. AGL believes, however, that these matters are material and the core issues discussed in this submission are consistent with those raised in its First Submission. The revised cost recovery approach, released by the Victorian Jurisdiction in late 2008, with no public consultation and after the Draft Rule Determination, reinforces and extends AGL's views on the issues raised on cost and contestability of AMI rollout in its First Submission.

Please contact me or Kong Min Yep on 0402 060 759 if you have any queries.

Yours sincerely,

A handwritten signature in blue ink, appearing to be 'Elizabeth Molyneux'.

pp Elizabeth Molyneux
General Manager Energy Regulation