



23 July 2010

Australian Energy Market Commission  
PO Box A2449  
Sydney South NSW 1235

## **EPR0018 DRAFT REPORT - REQUEST FOR ADVICE ON COST RECOVERY FOR MANDATED SMART METERING INFRASTRUCTURE**

### **Introduction**

Origin Energy Retail Limited (Origin) welcomes this opportunity to respond to the Commission's Draft Report on cost recovery of mandated smart metering infrastructure (SMI) roll-outs and pilots and trials.

As a large energy retailer in the National Electricity Market (NEM), Origin believes it is important to establish cost recovery mechanisms of mandated SMI to provide certainty for investors (generally distribution businesses) but equally, for customers as the party who will ultimately pay for a mandated SMI roll-out. Origin is also an active within the National Smart Metering Program (through the National Stakeholders Steering Committee and working groups).

In Victoria, Origin (along with other licensed retailers) has been responsible for the recovery of costs for the SMI roll-out since January 2010 on behalf of the distribution businesses responsible for deploying the new technology.

In general, we are supportive of the approach set out in the Draft Report, namely, the application of chapter 6 of the National Electricity (NER) Rules with as little modification as possible. Our support for this approach is based on:

- That under a mandate, robust cost benefit analysis and testing would have taken place leading to a conclusion that the provision of SMI should be exclusively provided by a monopoly provider;
- That given a decision to allow for exclusivity, the cost recovery of SMI should be treated in a similar way to conventional network infrastructure, noting that it may be made contestable in the future; and
- Chapter 6 provides a transparent framework and process enabling the regulator and market participants to assess the cost applications made by distributors when a decision to deploy mandated SMI is made.

Origin's previous submission on the Commission's Draft Statement of Approach also highlighted these views.<sup>1</sup>

Origin generally endorses the incremental amendments described by the Commission in page (i) of the Draft Report, recognising that the mandated deployment of SMI presents

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<sup>1</sup> See for example pages 1-2 and 4 of Origin's submission on the Draft Statement of Approach.



some challenges to traditional network regulation. Specific matters identified by the Commission are discussed below; however Origin does support the Commission's view that a Ministerial roll-out determination should be aligned with the start of a new distribution determination period. Such alignment will eliminate significant regulatory uncertainty and administrative costs for industry participants.

On page (v) of its summary, the Commission puts the view that unbundling of charges associated with SMI is preferred as a means of enhancing allocative efficiency and transparency of costs facing consumers funding a roll-out. The Commission goes on to suggest that such charges should not apply to customers until an installed and functioning smart meter is in place.

While Origin supports the unbundling of costs as recommended in the Commission's Draft Report, we do not believe it is practical to apply these charges only when SMI is installed and operating at individual premises.

In Victoria, SMI costs are allocated on a national metering identifier (NMI) basis or meter level basis. Given the large upfront investment that an accelerated roll-out of SMI would require, Origin does not agree that the costs should be applied only when a meter is installed and functioning. While we believe allocation of costs in this way may be appropriate where a commercial roll-out is undertaken (and customers agree and express a willingness to pay for SMI), once a decision is made to provide SMI on an exclusive basis, all customers within an affected region would be subject to cost recovery, whether or not a smart meter was installed.

In addition, there would be significant administrative costs for retailers and potentially the market operator if under exclusive mandated SMI provision costs were allocated to customers at the margin, or an incremental install basis.

Finally, while Origin recognises the focus of the Commission's Draft Report is for cost recovery of SMI where a mandate is declared, the mechanisms applied and rule changes that may take place will influence costs and benefits for customers following the end of any exclusive period of SMI provision. The MCE has indicated its policy preference to interoperability and to competition beyond a mandate period. The unbundling of the metering charges is a first and essential requirement for this policy outcome to be realised post mandate.

The remainder of this submission addresses selected issues raised by the Commission in its Draft Report. Origin would be pleased to discuss further matters raised in this response and the Draft Report with the Commission.

Regards

[SIGNED]

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## Specific comments

### *Cost recovery under the distribution determination process*

*Question 1: Cost recovery under the distribution determination process.*

*1.1 Should the AER be able to apply the proposed mechanisms to address remaining uncertainty (i.e. the roll-forward of the RAB on the basis of forecast depreciation and the cost sharing mechanism) to other distribution investments, where the potential costs and benefits of such investments are uncertain at the time a distribution determination is made?*

While Origin believes there is merit in applying the mechanisms proposed to other distribution investments, we do not believe this question is within the intended scope of the MCE request for advice.

*1.2 Do you consider that a specific information provision requirement should be included in the Rules to require DNSPs to provide annual information on the costs and operational benefits of mandated smart meter roll-outs, pilots and trials? Or do you consider that the AER's current information gathering powers under the NEL are sufficient?*

Annual reporting, particularly for a mandated jurisdictional roll-out may have merit, but it is important that the AER and users of such information understand that the benefits reported will be limited to those the network can reasonably identify. Other benefits will not be included and would be difficult to define. The management of any information provided by DNSPs (as the regulated party) should be considered carefully. For example, it may be provided to the AER only in assisting with its assessment of SMI costs. Any reporting of operational benefits achieved by a network would have to be heavily qualified as partial in nature only. Also, the regulatory cost to DNSPs of annual reporting should be considered.

Nevertheless, properly constructed, there may be some benefits of annual reporting. These include:

- General educational benefits;
- Confirmation of the cost-benefit assumptions that underpinned the network investment;
- Facilitate future determinations, including future capital investment requirements through more regular and consistent reporting across the current regulatory period.



*3.1 Are further amendments to the cost pass through provisions required to provide for the recovery of the efficient costs of mandated smart meter pilots and trials?*

In its Draft Finding 14, the Commission acknowledges that due to a lack of specification of criteria the AER would apply in making a cost pass through determination, the current NER provisions may not provide for the recovery of efficient retailer costs.

The proposed amendments for cost pass through processes set out in section 4.3.2 of the Draft Report go some way to addressing the uncertainty associated with the current assessment of third party costs. Certainty is required for third parties as a DNSP could engage a retailer and agree terms that would mean payment for services would be contingent on AER approval of retailer costs (for a pilot/trial for example). Given that even a modest pilot or SMI trial would impose significant costs on a retailer (for example, pricing, billing, market contract collateral etc), contingent terms for cost recovery would in likelihood discourage retailer participation.

While ultimately it is the AER's role to make a cost pass through determination, it should be understood that this decision would most likely need to be made prior to a retailer committing resources for a pilot or trial. Neither DNSPs nor retailers would be comfortable with such material uncertainty before commencement and during the execution of a SMI pilot or trial.

*Question 5: Incentives under the current regulatory regime*

*5.1 Are any changes to the Rules required to ensure the incentives under the current regulatory regime are appropriate for mandated SMI?*

Origin would like to address a number of issues that emerge in relation to current regulation following the conclusion of a mandated roll-out of SMI in relation to technology risk.

While we agree that the NSSC and MCE deliberations will address this issue, the Commission and the AER need to consider the incentives placed on distributors to optimise investment decisions where a mandated roll-out is to take place in the context of a known post mandate environment, which would likely include contestability.

To illustrate, in the case of SMI communications technology, if interoperability and open protocol standards were not selected by the DNSP under a mandate, the compensation for asset stranding (however achieved) should reflect the decision to choose technology incompatible with a known future state of contestability. Future changes to incentives contained in chapter 6, including the treatment of SMI assets in the Regulatory Asset Base may need to be considered to address these issues.

Again, while a critical consideration of investment decisions in the context of future states is relatively new concept in economic regulation, it is nevertheless an important feature of the decision making processes in terms of reconciling the concept of a mandated roll-out with the clear policy preference over the longer term for a competitive market in metering services.



*Question 6: Tariff issues associated with mandated SMI*

6.1 *What principles should the AER be required to have regard to for the efficient allocation of costs and in determining whether to require a DNSP to unbundle mandated smart metering services from DUOS charges?*

6.2 *Should Rules on the unbundling of mandated smart metering services be made at this time, in light of the current uncertainty regarding the future contestability of smart metering services?*

Origin again would indicate its support for the unbundling of SMI costs from general use of system charges. Our preference would be for unbundled SMI services (metering, data and other services as these evolve) to remain standard control services, noting present limitations in the rules. Ideally, combining the discipline of the building blocks approach to standard control services, but unbundling these from NUOS would be the most appropriate approach to SMI pricing.

We therefore support the second approach identified by the Commission on page 99 of the Draft Report, that is, amending the Rules to apply a principles based approach and furnish the AER with additional influence on the setting of tariffs for mandated smart meter services.

In relation to the SMI pricing principles described on page 100 of the Draft Report, Origin makes the following comments in the table below:

	<b>Suggested Principle</b>	<b>Comments</b>
1	Tariffs must be based on the costs incurred in providing the mandated smart metering service.	High level agreement with this principle. Difficulty arises in practice in addressing the services that are relevant.
2	The cost of providing mandated smart metering services should be recovered through a fixed tariff.	Due to the largely fixed cost nature of the metering assets, Origin generally agrees with this principle.
3	A proportion of the costs should be allocated to those customers who benefit from the mandated smart metering services, based on the share of benefits those customers receive compared to the benefits all customers receive.	Further consideration of this principle is required, including its impact on meter contestability following a period of exclusivity. In addition, the practical difficulties of applying this principle in the mass market should be carefully considered, particularly given that benefits will shift over time.
4	A proportion of the costs should be allocated to general DUOS tariffs, based on the share of benefits all customers receive compared to the benefits that are specific to customers with mandated smart meters.	There are implications following the end of an exclusive period of SMI and SMI service provision to address here.  Also see comments on 3 above.
5	The DNSP shall not be remunerated twice for the same cost through different tariffs.	Agree with this principle. Also, following a period of exclusive provision (e.g. during a roll-out), a customer who receives SMI from a separate service provider should not longer pay the DNSP either.
6	Promote future contestability in smart metering services.	We agree with this principle, but would emphasise that there are a range of services available. In Victoria, the AER has approved a single charge for metering services for the roll-out of Advanced Metering Infrastructure. While the cost is unbundled from DUOS, there is less transparency today than



	Suggested Principle	Comments
		previously, since meter data services (for basic or interval-read meters) and meter provision were separately priced service in the past. In practice, both physical meter provision and a range of services enabled by a smart meter could be provided by separate providers (including DNSPs) in a competitive environment.
7	Easily comprehensible.	Agreed.
8	Must be determined with regard to the transaction cost of calculating the tariff.	While this is an important consideration for DNSPs as developers of proposals, it should not be granted too much weight in the context of the benefits associated with the unbundling of SMI costs.

Origin believes that Rules to unbundle mandated SMI services (and provision) should be considered for metering services generally (not just where a mandated roll-out is promulgated) as there is the potential for contestability in most NEM jurisdictions today. Many of the elements of mandated SMI deployment are uncertain today, including future contestability. On this basis, Origin would not support the postponement of rules being established in relation to unbundling and believes the Commission has set out sound reasons for doing so summarised in Draft Finding 25.