



20 June 2017

Office of the  
Chief Executive Officer

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Australian Energy Market Commission  
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Dear Mr Pierce

***Ausgrid's submission on AEMC's draft rule determination on participant derogation – NSW DNSPs revenue smoothing – ERC0210***

Ausgrid welcomes the opportunity to provide this submission on the AEMC's draft rule determination on the participant derogation on revenue smoothing that the NSW DNSPs submitted.

We are fully supportive of the AEMC's decision to make a Rule that allow for the smoothing of revenue between regulatory periods to ensure price stability for customers. We agree with the AEMC that making such a Rule is in the long term interest of customers.

However we consider that certain aspects of the Rule, as currently drafted, can be improved to provide clarity and certainty in scope for the NSW DNSPs and the AER, the parties implementing the Rule when it is made. Our submission is therefore focused solely on the technical aspects of implementing the requirements of the Rule with the aim to ensure that final Rule, when made, would operate as intended in a transparent and balanced manner and that it can be implemented without any ambiguity.

We consider that this is critical as it is possible that the Rule would not be implemented for a number of months. This is because the Rule cannot take effect until the current situation regarding the AER's distribution determination for the NSW DNSPs for the 2014-19 period is resolved.

Our submission outlines the principles that should guide that operation of the Rule and based on these principles sets out:

- The mechanism for identifying the revenue amounts (increment or decrement) that, if left unsmoothed, would result in price shocks for customers.
- The allocation of that revenue amount between regulatory periods (i.e. the smoothing) and the principles that the AER should have regard to in making this decision.

In Attachment 1 to this submission, we outlined the guiding principles that we consider the Rule should give effect to and some observations on the current drafting of the Rule. These guiding principles underlie the changes we have suggested to the AEMC's drafting.

Attachment 2 provides Ausgrid's suggested marked-up changes to the Rule as currently drafted. Attachment 3 explains the alternate wordings and how we consider these should work in practice.

I understand officers from the AEMC, AER and NSW DNSPs have met on a number of occasions to discuss and refine the working of the participant derogation. We appreciate these opportunities and the collaboration of all parties. At the most recent meeting, officers of the NSW DNSPs and the AER indicated that agreed orders had been filed with the Federal Court with respect to the recent decision of the Federal Court on the AER's judicial review application. If made, those orders will impact on the scenarios contemplated by the Rules. Ausgrid's officers will be in touch with the Commission as soon as the outcome of the orders process is known.

We would appreciate the opportunity to discuss our proposed changes as well as the opportunity to review any further draft of the Rule before the AEMC's final determination is published. Please contact Rob Amphlett Lewis, Executive General Manager – Strategy & Regulation, on (02) 9269 4501 or via email at [rob.amphlettlewis@ausgrid.com.au](mailto:rob.amphlettlewis@ausgrid.com.au)

Yours sincerely



**RICHARD GROSS**

Chief Executive Officer

## Attachment 1: Principles, observations and recommendation

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In this attachment we set out:

1. The principles we consider are fundamental to the operation of the Rule.
2. The observations we have on the AEMC's Rule as currently drafted.
3. Our recommendation for alternate wordings.

Attachment 2 shows the proposed changes in marked-ups. In attachment 3, we set out in detail how the proposed alternate definitions and provisions should work in practice.

### **a. Guiding principles for the Rule**

The over-arching objective of the participant derogation / proposed Rule that the NSW DNSPs sought, and of the Draft Rule that the AEMC has made, is to ensure that consumers do not experience a price shock. The price shock results from the current Rules which anticipate all revenue for a regulatory control period being recovered within the regulatory control period. Consequently, recovering a significant revenue amount (increment/decrement) which might arise from a remade determination within the short timeframe left in the current regulatory period would cause price spikes. A change to the way in which the rules operate is consequently needed to allow the recovery of revenue over a longer period to smooth out price volatility.

It is therefore critical that the operation of the Rule, when made, reflects and is faithful to this underlying driver that gave rise to the need for it. That is:

1. The NSW DNSPs are not entitled to recover any more revenue than they are entitled to as determined by the AER under a remade distribution determination. This principle is analogous to the control mechanism imposed by the AER (i.e. revenue cap form of control) under which DNSPs can only recover revenue up to the cap imposed by the AER.

Additional to this fundamental principle are other guiding principles that are necessary for an effective Rule and these are:

2. The NSW DNSPs should not be deprived of the opportunity to fully recover their respective revenue entitlements for the 2014-19 period if revenues are spread over two regulatory periods.
3. The Rule, when made, is workable and can be understood and implemented by all parties without any ambiguity. For this to be the case, the Rule should minimise any potential for different interpretations.

### **b. Why current drafting of proposed Rule does not fully give effect to the above principles and could be more transparent**

We understand that the above principles are not disputed by any parties involved in the drafting of the Rule as well as in the implementation of the Rule when made. Rather, the key matter to resolve and to be agreed upon is the implementation of the Rule which in essence involves two fundamental aspects:

- (a) the calculation of the amount of revenue in the AER's remade determination that places the NSW DNSPs in the same position as if the remade determination was in place at the beginning of the regulator period (i.e. make 'whole') and

(b) the recovery period of this amount (the period over which the smoothing process is to take place) and whether it takes place over the last year of the current period and next period or wholly in the next period.

As currently drafted, the definition of 'adjustment amount' is very broad and provides no guidance as to how the revenue increment/decrement is to be determined other than that the AER must determine the adjustment amount that it is satisfied would be 'reasonably likely to minimise variations in use of system charges'. All the detail of the calculation of the amount and the basis for it is left to the AER's discretion. This is unsatisfactory in terms of transparency and objectivity and may give rise to unnecessary disputes.

In assessing the workability of the Rule as drafted, the following questions arose:

1. Why the definition (and the definition of 'variation amount') refers only to final regulatory year of the current period when a remade distribution determination would affect the revenue for all years of the regulatory control period? For example, a re-determination by the AER on the cost of debt would affect the revenue of all years of the regulatory control period.

Under the current definitions of adjustment amount and variation amount, while the AER may determine that any difference in allowed revenues across the current regulatory control period under a remade 2015 determination should be applied in the final year (allowing any difference to be reflected in prices for the final regulatory year) it is not required to do so. Such open-ended discretion only creates regulatory uncertainty and we consider does not satisfy the 'make whole' principle. We discuss below, and in attachment 3, our proposed alternate definitions.

2. What is the relevance of the reference to 'control mechanism' in the definition (and in the definition of variation amount)? What role does this term play in the current definitions?

The inclusion of the term 'control mechanism' in the definition causes confusion. The control mechanism determines how prices and/or revenue are controlled over a regulatory period. It does not determine the amount of revenue that is allowed to be recovered over the regulatory period or permit the recovery of revenue between periods. It is the formulae that give effect to the control mechanism (control mechanism formulae) determined by the AER and the application of those formulae that are relevant to the setting of the amount of revenue that DNSP is entitled to recover from customers in the annual price setting.

3. It is not clear if the definitions of 'adjustment amount' and 'variation amount' as currently drafted cater for the actual revenue collected or expected to be collected to date. It is also not clear if the adjustment amount is intended to be net present value neutral.
4. What is the relationship between the terms 'total annual revenue' and the phrase 'the annual revenue requirement and control mechanism'?
5. How does the current definition cater for the consequential impact of remade revenue on the calculation of incentive schemes outcomes that would have applied during the period?

The above were the immediate questions that arose as we considered the definitions as currently drafted. It was only after having discussions with the AEMC's officers that we were able to understand the nuances of the current drafting. In this respect, the current draft of the Rule requires many underlying assumptions to be workable and therefore is susceptible to different interpretations. That is not a desirable outcome. This is because:

- a. The Rule as currently drafted would require an inherent assumption and common understanding by all parties that the AER would:

- i. First, make a new determination which accounts for all the revenues that the NSW DNSPs are entitled to including all revenue entitlements / refunds under applicable incentive schemes and post determination adjustments.<sup>1</sup> These are all the adjustments that would have occurred as a matter of course if a valid determination was in place.
  - ii. Second, compare that amount to revenue actually collected or expected to be collected to date to arrive at the 'final year' year revenue that would ensure the DNSPs do not recover more or less than the revenue entitlement.<sup>2</sup>
  - iii. Then, from this final year revenue the AER would determine an amount (increment/decrement) to adjust the final year revenue to minimise price volatility. This adjusted final year revenue becomes the 'substituted total annual revenue amount' for pricing purposes.
- b. Consequently, the Rule as currently drafted results in a process that is not as transparent and workable as it can be. It does not lend itself readily to a prima facie confirmation that the principle of 'make whole' is being adhered to. For example, in the current drafting of the 'variation amount', the AER has the discretion to account for all the necessary adjustments pertaining to years 1 to 4 in year 5 of the 2014-19 period but it is not required to do so.<sup>3</sup> This leaves the current drafting open to uncertainty and potentially dispute. Consequently, faithfulness to the principle of 'make whole' under the Rule as currently drafted would entail the specific steps outlined above to be complied with by the AER.
- c. The current drafting also subsumes the determination of an adjustment amount and allocation/deferral of that amount to the next period in one process/step. That is, the AER would, in one process/step, decide that revenue deferral is needed and then calculate how much revenue needs to be deferred.
- d. The Rule as currently drafted utilises two definitions, being adjustment amount and variation amount, depending on the scenario applicable. This is because the current Rule subsumes two distinct processes into one, i.e. the calculation of the revenue amount (increment or decrement) needed to keep the NSW DNSPs whole and the allocation of that amount across period to ensure no price shocks. For example, in scenario 2 and 3, there is no need to allocate the revenue amount across periods because the time to do so has passed, the only issue then is the determination of the amount (belonging to the current period) that is to be recovered in the next regulatory period.

### **c. Ausgrid's recommendation**

In our view, the calculation of the revenue amount that places the DNSPs in the same position as they would have been had the remade determination been made at the time of the final determination and had the control mechanism formula been implemented for the relevant year of the regulatory control period should be an objective and mechanical exercise. It is therefore more transparent and easier to understand and implement if the Rule giving effect to the objective of the participant derogation is split into two distinct steps:

- a. The calculation of the revenue amount needed to ensure that NSW DNSPs are kept whole. This amount could either (a) be recovered in the final year of the 14-19 period in which case such recovery may cause price shocks and consequently requires the AER to determine how much of this revenue amount is to be deferred to the next period or (b) if the time for recovering in the final year has passed, be included in the next period determination and recovered accordingly.

Our amendment proposes that this calculation is done by reference to the total revenue that the AER determined under the remade decision and the actual revenue Ausgrid collected or expects

<sup>1</sup> Ausgrid understands from discussion with the AEMC that this is implied from the expression '*annual revenue requirement and control mechanism*' in the definitions of adjustment amount and variation amount.

<sup>2</sup> Ausgrid understands from discussion with the AEMC that this is implied by the reference to the expression '*for the final regulatory year of the current regulatory control period*' in the definitions of adjustment amount and variation amount.

<sup>3</sup> For example, if there is a change to the cost of debt, it will impact all years of the regulatory period, not just the final year.

to collect to date<sup>4</sup>. In addition our alternate draft of the Rule proposes to use only one term ('adjustment amount') as opposed to two under the current draft and this single term can be applied to all three scenarios identified in the AEMC's draft determination. We consider this will aid in simplicity, transparency and workability.

Attachment 2 shows proposed amendments to the various clauses of the draft Rule. Attachment 3 sets out in detail how this calculation operates and the scope of the various alternate definitions we proposed.

- b. The split of this revenue (as calculated in (a) above) between amounts to be recovered in the current period and subsequent period. The determination of this split is to be based on principles of:
1. Reasonably likely to minimise variations in charges between regulatory years and regulatory periods.
  2. Permitting the DNSP to fully recover the revenue determined by the AER.

The first principle is self-explanatory as it is the over-arching objective of the proposed participant derogation, i.e. minimising price volatility for customers. Attachment 3 explains principle 2.

In making the proposed amendments, we took the approach of ensuring that the Rule, when made, is as clear as possible and to the greatest extent should leave no room for dispute or ambiguity. This can be achieved by setting out the exact steps/method for calculating the revenue amount and the scope of this amount (i.e. what each step includes or does not include). We consider that this approach neither restricts the discretion of the AER nor is inappropriately prescriptive. We consider it is consistent with other provisions in Chapter 6 of the NER that set out how a particular amount is to be calculated. For example:

- Schedule 2 of the NER sets out step by step how the regulatory asset base (RAB) should be rolled forward from one regulatory year to the next and from one regulatory period to another. This schedule specifies what should be added (capex) and deducted (depreciation and disposal).
- Similarly, clause 6.5.3 of the NER sets out the exact formula for calculating the estimated cost of income tax.

Our proposed amendments adopt the same approach of setting out the formulaic way in which the adjustment amount should be calculated and therefore accords with current regulatory practice with respect to the calculation of amounts.

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<sup>4</sup> Or in Ausgrid's case, the Maximum Allowed Revenue (MAR) for dual function assets that were used in TransGrid's TUOS price setting process each year.

## **Draft National Electricity Amendment (Participant derogation - NSW DNSPs Revenue Smoothing) Rule 2017**

### **1 Title of Rule**

This Rule is the *Draft National Electricity Amendment (Participant derogation - NSW DNSPs Revenue Smoothing) Rule 2017*.

### **2 Commencement**

This Rule commences operation on [COMMENCEMENT\_DATE].

### **3 Amendment of the National Electricity Rules**

The National Electricity Rules are amended as set out in Schedule 1.

## Schedule 1 Amendment to the National Electricity Rules

(Clause 3)

### [1] Chapter 8A New Part 14

In Chapter 8A, after Part 13, insert:

#### Part 14 Derogations granted to Ausgrid, Endeavour Energy and Essential Energy

##### 8A.14 Derogations from Chapter 6 for the current regulatory control period and subsequent regulatory control period

###### 8A.14.1 Definitions

In this *participant derogation*, rule 8A.14:

**2015 determination**, in respect of each NSW DNSP, means the following applicable distribution determination:

- (a) the distribution determination for the current regulatory control period published by the *AER* on 30 April 2015 (as corrected in accordance with the *AER's* letter dated 20 May 2015) in respect of Ausgrid;
- (b) the distribution determination for the current regulatory control period published by the *AER* on 30 April 2015 (as corrected in accordance with the *AER's* letter dated 20 May 2015) in respect of Endeavour Energy; and
- (c) the distribution determination for the current regulatory control period published by the *AER* on 30 April 2015 (as corrected in accordance with the *AER's* letter dated 20 May 2015) in respect of Essential Energy.

**adjustment amount** in respect of a NSW DNSP, means an amount ~~that operates as if it were~~ equivalent in net present value terms to the difference between:

(a) ~~– a revenue increment~~ the current allowed revenue; and

(b) the current actual revenue ~~– a revenue decrement,~~

as at the regulatory year in which the adjustment determination is made, provided that:

(c) if the adjustment amount is positive, it will be a revenue increment;  
and

(d) if the adjustment amount is negative, it will be a revenue decrement.  
~~to the total annual revenue that may be earned by that NSW DNSP~~



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~~for the final regulatory year of the current regulatory control period in accordance with the *annual revenue requirement* and control mechanism that apply under:~~

~~(c) if clause 8A.14.4(a)(1) applies, the remade 2015 determination; or~~

~~(d) if clause 8A.14.4(a)(2) applies, the affirmed or varied 2015 determination.~~

**adjustment determination** means the *AER's* determination:

- (a) under clause 8A.14.4, of any, and the relevant amounts of the, adjustment amount, current adjustment amount and subsequent adjustment amount; and
- (b) under clauses 8A.14.5 and 8A.14.6, the relevant amounts of the ~~variation amount and subsequent~~ adjustment amount.

**affirms or varies the 2015 determination** means the Tribunal affirms or varies the 2015 determination under section 71P(2)(a) or (b) of the *National Electricity Law*, respectively, or any other relevant power of the Tribunal, and makes no concurrent order to set aside and remit the matter back to the *AER* under section 71P(2)(c) of the *National Electricity Law* or under any other relevant power of the Tribunal.

**Ausgrid** means ~~Ausgrid, the energy services corporation of that name (formerly known as EnergyAustralia), which is constituted under section 7 of the *Energy Services Corporations Act 1995* (NSW) and specified in Part 2 of Schedule 1 of that Act, or any successor to its business (including any 'authorised distributor' of Ausgrid's 'network infrastructure assets' (as those terms are defined in the *Electricity Network Assets (Authorised Transactions) Act 2015* (NSW)) following the transfer of the whole, or part, of those network infrastructure assets to the private sector);~~ the Ausgrid Operator Partnership (ABN 78 508 211 731) of 570 George Street, Sydney NSW 2000 comprising of:

- (a) Blue Op Partner Pty Ltd (ACN 615 217 500) as trustee for the Blue Op Partner Trust;
- (b) ERIC Alpha Operator Corporation 1 Pty Ltd (ACN 612 975 096) as trustee for ERIC Alpha Trust 1;
- (c) ERIC Alpha Operator Corporation 2 Pty Ltd (ACN 612 975 121) as trustee for ERIC Alpha Trust 2;
- (d) ERIC Alpha Operator Corporation 3 Pty Ltd (ACN 612 975 185) as trustee for ERIC Alpha Operator Trust 3; and
- ~~(a)~~(e) ERIC Alpha Operator Corporation 4 Pty Ltd (ACN 612 975 210) as trustee for ERIC Alpha Operator Trust 4.

**current actual revenue** means the sum of revenue actually earned or expected to be earned in each previous and current regulatory year of the current regulatory control period. In the case of revenue for the services provided by dual function assets, the revenue used in the setting of transmission use of system charges by TransGrid in each previous and current regulatory year of the current regulatory control period.

**current adjustment amount**, in respect of a NSW DNSP, means that proportion of the adjustment amount determined by the *AER* to apply in the current regulatory control period under clause 8A.14.4(c).

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**current allowed revenue** means the sum of:

- a) the annual revenue requirements approved by the AER in the remade 2015 determination for each previous or current regulatory year of the current regulatory control period, and
- b) revenue adjustments required to effect the application of the control mechanism formulae in each relevant year of the current regulatory control period.

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**current regulatory control period**, for each NSW DNSP, means the period of five years that commenced on 1 July 2014 and ends on 30 June 2019, which includes the 'transitional regulatory control period' and 'subsequent regulatory control period' as those terms are defined in clause 11.55.1.

**Endeavour –Energy** means –

the Endeavour Energy Network Operator Partnership (ABN 11 247 365 823) of 51 Huntingwood Drive, Huntingwood NSW 2148 comprising of:

(f) Edwards O Pty Limited (ACN 618 643 486) as trustee for the Edwards O Trust;

(g) ERIC Epsilon Operator Corporation 1 Pty Ltd (ACN 617 221 735) as trustee for ERIC Epsilon Operator Trust 1;

(h) ERIC Epsilon Operator Corporation 2 Pty Ltd (ACN 617 221 744) as trustee for ERIC Epsilon Operator Trust 2;

(i) ERIC Epsilon Operator Corporation 3 Pty Ltd (ACN 617 221 753) as trustee for ERIC Epsilon Operator Trust 3; and

(j) ERIC Epsilon Operator Corporation 4 Pty Ltd (ACN 617 221 771) as trustee for ERIC Epsilon Operator Trust 4.

~~Endeavour –Energy, (ABN 59 253 130 878) of 51 Huntingwood Drive, Huntingwood NSW 2148, the energy services corporation of that name (formerly known as Integral Energy), which is constituted under section 7 of the *Energy Services Corporations Act 1995* (NSW) and specified in Part 2 of Schedule 1 to that Act, or any successor to its business (including any 'authorised distributor' of Endeavour Energy's 'network infrastructure assets' (as those terms are defined in the *Electricity Network Assets (Authorised Transactions) Act 2015* (NSW)) following the transfer of the whole, or part, of those network infrastructure assets to the private sector).~~

**Essential Energy** means Essential Energy, the energy services corporation of that name (formerly known as Country Energy), which is constituted under section 7 of the *Energy Services Corporations Act 1995* (NSW) and specified in Part 2 of Schedule 1 of that Act, or any successor to its business.

**NSW DNSP** means each of the following *Distribution Network Service Providers*:

- (a) Ausgrid;
- (b) Endeavour Energy; and
- (c) Essential Energy.

**regulatory year** means each consecutive period of 12 calendar months in the current regulatory control period or subsequent regulatory control period (as the case may be) (the current regulatory control period and subsequent regulatory control period each being a **regulatory control period**), the first such 12 month period commencing at the beginning of the regulatory control period and the final 12 month period ending at the end of the regulatory control period.

**remade 2015 determination**, in respect of each NSW DNSP, means the 2015 determination of that NSW DNSP as remade by the *AER* following the Tribunal's decision.

**scheme**, in respect of each NSW DNSP, means the efficiency benefit sharing scheme, the capital expenditure sharing scheme, the service target performance incentive scheme and the demand management incentive scheme applying to that NSW DNSP at the relevant time.

**subsequent adjustment amount**, in respect of a NSW DNSP, means an amount that is equivalent in net present value terms to the amount that is equal to the adjustment amount less the current adjustment amount: (a) ~~if clause 8A.14.4 applies, an amount that:~~

- ~~(1) is equivalent in net present value terms to the adjustment amount; and~~
- ~~(2) represents a revenue increment (where the adjustment amount is a negative amount) or a revenue decrement (where the adjustment amount is a positive amount) to the annual revenue requirement of the first regulatory year of the subsequent regulatory control period; or~~
- ~~(b) if clause 8A.14.5 applies, an amount that is equivalent in net present value terms to the variation amount; or~~
- ~~(c) if clause 8A.14.6 applies, an amount that is equivalent in net present value terms to the variation amount.~~

**subsequent distribution determination**, in respect of each NSW DNSP, means the distribution determination of that NSW DNSP made by the *AER* for the subsequent regulatory control period.

**subsequent regulatory control period**, in respect of a NSW DNSP, means the *regulatory control period* for that NSW DNSP that immediately follows the current regulatory control period.

**substituted total annual revenue amount** has the meaning given in clause 8A.14.4(d).

~~**total annual revenue**, in respect of a NSW DNSP, means the total revenue that the NSW DNSP is entitled to earn from the provision of *standard control services* for the relevant regulatory year.~~

**Tribunal** means the Australian Competition Tribunal.

**Tribunal's decision** means the decision of the Tribunal in relation to the 2015 determination of each NSW DNSP delivered on 26 February 2016, as varied or remade as a consequence of the outcome of the judicial review of that decision.

~~**undertaking**, in respect of a NSW DNSP, means an undertaking given to, and approved by, the *AER* under section 59A of the *National Electricity Law* in respect of the revenue earned and/or prices charged by that NSW DNSP for the relevant regulatory year.~~

~~**variation amount**, in respect of a NSW DNSP, means:~~

~~(a) — if clause 8A.14.5 applies, an amount equivalent to the difference between the total annual revenue for the NSW DNSP for the final regulatory year of the current regulatory control period under:~~

~~(1) — if clause 8A.14.5(a)(1) applies:~~

~~(i) — the *annual revenue requirement* and control mechanism under the remade 2015 determination; and~~

~~(ii) — any undertaking that applies for that regulatory year,~~

~~provided that if the total annual revenue under the undertaking is greater than the total annual revenue under the remade 2015 determination, the variation amount will be a negative amount; or~~

~~(2) — if clause 8A.14.5(a)(2) applies:~~

~~(i) — the *annual revenue requirement* and control mechanism under the affirmed or varied 2015 determination (as applicable); and~~

~~(ii) — any undertaking that applies for that regulatory year,~~

~~provided that if the total annual revenue under the undertaking is greater than the total annual revenue under the varied or affirmed 2015 determination (as applicable), the variation amount will be a negative amount; or~~

~~(b) — if clause 8A.14.6 applies, an amount equivalent to the difference between the total annual revenue for the NSW DNSP for the final regulatory year of the current regulatory control period under:~~

~~(1) if clause 8A.14.6(a)(1) applies:~~

~~(i) the annual revenue requirement and control mechanism under the remade 2015 determination; and~~

~~(ii) any undertaking that applies for that regulatory year, provided that if the total annual revenue under the undertaking is greater than the total annual revenue under the remade 2015 determination, the variation amount will be a negative amount; or~~

~~(2) if clause 8A.14.6(a)(2) applies:~~

~~(i) the annual revenue requirement and control mechanism under the affirmed or varied 2015 determination (as applicable); and~~

~~(ii) any undertaking that applies for that regulatory year, provided that if the total annual revenue under the undertaking is greater than the total annual revenue under the varied or affirmed 2015 determination (as applicable), the variation amount will be a negative amount.~~

## 8A.14.2 Expiry date

This *participant derogation* expires on the date that immediately follows the end of the subsequent regulatory control period.

### ~~8A.14.3~~

### 8A.14.3 Application of Rule 8A.14

- (a) This *participant derogation* prevails to the extent of any inconsistency with any other provision of the *Rules*.
- (b) Nothing in this *participant derogation* has the effect of:
  - (1) changing the application of the *Rules* to the making of a remade 2015 determination; or
  - (2) rendering a change, in whole or in part, to the terms of a distribution determination that applies in respect of the current regulatory control period.
- (c) To the extent of any inconsistency between this *participant derogation* and a:
  - (1) remade 2015 determination; or
  - (2) 2015 determination affirmed or varied by the Tribunal,this *participant derogation* prevails.

#### 8A.14.4 Recovery of revenue across the current regulatory control period and subsequent regulatory control period

##### General

- (a) This clause 8A.14.4 applies in respect of a NSW DNSP if:
- (1) a remade 2015 determination is made by the AER in respect of that NSW DNSP prior to 1 March 2018; or
  - (2) the Tribunal affirms or varies the 2015 determination in respect of that NSW DNSP prior to 1 December 2017.

##### Adjustment determination

- (b) The AER may:
- (1) if subparagraph (a)(1) applies, determine at the time of making the remade 2015 determination; or
  - (2) if subparagraph (a)(2) applies, determine by 28 February 2018,

for the relevant NSW DNSP, an adjustment amount;

- ~~(3c)~~ -When determining an adjustment amount the AER must be satisfied that the adjustment determination will result in the relevant NSW DNSP's allowed revenue being the same (in net present value terms) as it would have been if the remade 2015 determination had been in place from the commencement of the current regulatory period and the control mechanism and control mechanism formulae specified in the remade 2015 determination had applied in each relevant regulatory year.

- ~~(d)~~ If the AER has determined an adjustment amount under paragraph (b) it must determine on a net present value equivalent basis an adjustment amount;

~~(1)~~ a current adjustment amount to apply in the current regulatory control period; and

~~(2)~~ a subsequent adjustment amount to apply in the subsequent regulatory control period,

~~if the AER is satisfied that the application of the adjustment amount and subsequent adjustment amount under paragraphs (d) and (e), respectively,~~

~~(1)~~ are ~~would be~~ reasonably likely to minimise variations in use of system charges:

~~(5)~~ —(i) ~~between~~ the penultimate and final regulatory years of the current regulatory control period; and



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~~(6)~~ (ii) between the final regulatory year of the current regulatory control period and the first regulatory year of the subsequent regulatory control period,

for the relevant NSW DNSP; and

~~(23)~~ will provide the NSW DNSP with an opportunity to fully recover the revenue allowed under the remade 2015 determination, or affirmed or varied 2015 determination.

**Note:**

When determining the adjustment amount and subsequent adjustment amount, the *AER* must also take into account the *national electricity objective* and may take into account the revenue and pricing principles: see *National Electricity Law*, s.16(1)(a) and (2)(b).

~~(ee)~~ Paragraphs ~~(df)~~ and ~~(eg)~~ do not apply in respect of a NSW DNSP if the *AER* has not determined an adjustment amount, ~~and current adjustment amount and~~ subsequent adjustment amount under paragraphs ~~(b) and (c)~~ for that NSW DNSP.

### Recovery in current regulatory control period

(~~f~~d) A pricing proposal submitted by a NSW DNSP, and approved by the AER, for the final regulatory year of the current regulatory control period must only provide for the recovery of:

(1) where the ~~applicable-current~~ adjustment amount operates as if it were a revenue increment:

(i) the NSW DNSP's ~~total annual~~ revenue ~~in accordance with the annual revenue requirement and control mechanism under allowed to be recovered under~~ the distribution determination in force for the final regulatory year of the current regulatory control period; plus

(ii) the ~~current~~ adjustment amount; or

(2) where the ~~applicable-current~~ adjustment amount operates as if it were a revenue decrement:

~~(i)~~ (i) — the NSW DNSP's ~~total annual~~ revenue ~~in accordance with the annual revenue requirement and control mechanism allowed to be recovered~~ under the distribution determination in force for the final regulatory year of the current regulatory control period; minus

~~(+)(ii)~~ ~~the current adjustment amount,~~

~~(ii)~~ ~~the adjustment amount,~~

(such amount being the **substituted total annual revenue amount**).

### Recovery in subsequent regulatory control period

(~~g~~e) The AER must include the subsequent adjustment amount determined for a NSW DNSP under paragraph (~~b~~c) as:

(1) if subparagraph (~~d~~f)(1) applies, a revenue ~~de~~crement; or

(2) if subparagraph (~~d~~f)(2) applies, a revenue ~~de~~crement,

to the *annual revenue requirement* determined under rule 6.4 for the first regulatory year of that NSW DNSP's subsequent regulatory control period.

(h) Any subsequent adjustment amount applied as a revenue increment or revenue decrement in the subsequent regulatory control period pursuant to paragraph (g) may not be considered by the AER when assessing whether any amount is payable or recoverable by the NSW DNSP under any scheme in the subsequent control period.

**8A.14.5 Recovery of revenue in subsequent regulatory control period only and no reopening of subsequent distribution determination required**

**General**

- (a) This clause 8A.14.5 applies in respect of a NSW DNSP if:

- (1) a remade 2015 determination is made by the *AER* in respect of that NSW DNSP on or after 1 March 2018, but prior to 1 February 2019; or
- (2) the Tribunal affirms or varies the 2015 determination in respect of that NSW DNSP on or after 1 December 2017, but prior to 1 February 2019.

#### **Adjustment determination**

(b) The *AER* must:

~~(1) (1)~~—if subparagraph (a)(1) applies, determine at the time of making the remade 2015 determination; or

~~(2)~~ if subparagraph (a)(2) applies, determine by 31 March 2019,

~~the variation adjustment amount and subsequent adjustment amount~~ for the relevant NSW DNSP.

(c) When determining an adjustment amount the AER must be satisfied that the adjustment determination will result in the relevant NSW DNSP's allowed revenue being the same (in net present value terms) as it would have been if the remade 2015 determination had been in place from the commencement of the current regulatory period and the control mechanism and control mechanism formulae specified in the remade 2015 determination had applied in each relevant regulatory year.

#### **Recovery in subsequent regulatory control period**

~~(d) The AER must include an amount that is equivalent in net present value terms to the adjustment amount determined for a NSW DNSP under paragraph (b) as:~~

~~(1) if the applicable adjustment amount is a positive amount, a revenue increment; or~~

~~(2) if the applicable adjustment amount is a negative amount, a revenue decrement,~~

~~(e) The AER must include the subsequent adjustment amount determined for a NSW DNSP under paragraph (b) as:~~

~~(1) if the applicable variation amount is a positive amount, a revenue increment; or~~

~~(2) if the applicable variation amount is a negative amount, a revenue decrement,~~

to the *annual revenue requirement* determined under rule 6.4 for the first regulatory year of that NSW DNSP's subsequent regulatory

control period.

- (e) Any subsequent adjustment amount applied as a revenue increment or revenue decrement in the subsequent regulatory control period pursuant to paragraph (c) may not be considered by the AER when assessing whether any amount is payable or recoverable by the NSW DNSP under any scheme in the subsequent control period.

**8A.14.6 Recovery of revenue in subsequent regulatory control period only and reopening of distribution determination is required**

**General**

- (a) This clause 8A.14.6 applies in respect of a NSW DNSP if:
  - (1) a remade 2015 determination is made by the *AER* in respect of that NSW DNSP; or
  - (2) the Tribunal affirms or varies the 2015 determination in respect of that NSW DNSP,

on or after 1 February 2019, but prior to 1 December of the fourth last regulatory year of the subsequent regulatory control period.

### Adjustment determination

(b) The *AER* must:

- (1) if subparagraph (a)(1) applies, determine at the time of making the remade 2015 determination; or
- (2) if subparagraph (a)(2) applies, determine by 28 February of the fourth last regulatory year of the subsequent regulatory control period,

the ~~variation-adjustment~~ amount and ~~subsequent-adjustment-amount~~ for the relevant NSW DNSP.

(c) When determining an adjustment amount the AER must be satisfied that the adjustment determination will result in the relevant NSW DNSP's allowed revenue being the same (in net present value terms) as it would have been if the remade 2015 determination had been in place from the commencement of the current regulatory period and the control mechanism and control mechanism formulae specified in the remade 2015 determination had applied in each relevant regulatory year.

### Recovery in subsequent regulatory control period

~~(d)~~ If paragraph (a) applies in respect of a NSW DNSP, the *AER* must revoke the subsequent distribution determination of that NSW DNSP and make a new distribution determination in substitution for that revoked determination, that:

- (1) applies to the remainder of the subsequent regulatory control period; and
- (2) includes ~~an amount that is equivalent in net present value terms to the the subsequent~~ adjustment amount for that NSW DNSP as:
  - (i) if the ~~applicable variation-adjustment~~ amount is a positive amount, a revenue increment; or
  - (ii) if the ~~applicable variation-adjustment~~ amount is a negative amount, a revenue decrement,

to the *annual revenue requirement* of one or more of the regulatory years for the remainder of the subsequent regulatory control period, subject to the aggregate of all such increases or decreases for the relevant regulatory years being equivalent in net present value terms to the ~~subsequent~~ adjustment amount.

~~(e)~~ Subject to paragraph (e), ~~T~~the substituted distribution determination made under paragraph (c) must only:

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- (1) vary from the revoked distribution determination to the extent necessary to reflect the increase or decrease (as the case may be) to the *annual revenue requirement* of one or more of the regulatory years for the subsequent regulatory control period under paragraph (c); and
- (2) be made after the *AER* has first consulted with the relevant NSW DNSP and such other persons as the *AER* considers appropriate.

- (f) Any subsequent adjustment amount applied as a revenue increment or revenue decrement in the subsequent regulatory control period pursuant to paragraph (c) may not be considered by the AER when assessing whether any amount is payable or recoverable by the NSW DNSP under any scheme in the subsequent control period.
- (g) If the AER revokes and substitutes the subsequent distribution determination under paragraph (c), that revocation and substitution must take effect from the commencement of the next regulatory year.

#### **8A.14.7 Requirements for adjustment determination**

The AER must:

- (a) make the adjustment determination after consulting with the relevant NSW DNSP and any other persons as the AER considers appropriate;
- (b) *publish* its adjustment determination:
  - (1) if clause 8A.14.4(a)(1), 8A.14.5(a)(1) or 8A.14.6(a)(1) applies, at the time of publication of the remade 2015 determination;
  - (2) if clause 8A.14.4(a)(2) applies, by 28 February 2018;
  - (3) if clause 8A.14.5(a)(2) applies, by 31 March 2019; or
  - (4) if clause 8A.14.6(a)(2) applies, by 28 February of the fourth last regulatory year of the subsequent regulatory control period; and
- (c) include in its adjustment determination, the reasons for the AER's determination of:
  - (1) if clause 8A.14.4 applies, the adjustment amount, current adjustment amount —and subsequent adjustment amount or, where the AER has not determined an adjustment amount, current adjustment amount and subsequent adjustment amount, the reasons for that decision; or
  - (2) if clause 8A.14.5 or 8A.14.6 applies, the ~~variation-adjustment amount~~ and subsequent adjustment amount.

#### **8A.14.8 Application of Chapter 6 under participant derogation**

- (a) Except as otherwise specified in this rule 8A.14 or Chapter 11, Chapter 6 applies to:
  - (1) the remainder of the current regulatory control period; and



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- (2) the making of a subsequent distribution determination,  
in respect of each NSW DNSP.
- (b) For the purposes of the application of clauses 8A.14.4, 8A.14.5 and 8A.14.6 (as applicable) in respect of a NSW DNSP, Chapter 6 is

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amended for the remainder of the current regulatory control period as follows:

- (1) clause 6.18.1A(c) does not apply to the extent necessary to allow for the submission of a *pricing proposal* by a NSW DNSP, and subsequent approval of such *pricing proposal* by the AER, in accordance with clause 8A.14.4(~~ef~~);
- (2) if clause 8A.14.4 applies, if any variation in proposed tariffs occurs as a result of:
  - (i) if clause 8A.14.4(a)(1) applies, the remade 2015 determination; or
  - (ii) if clause 8A.14.4(a)(2) applies, the affirmed or varied 2015 determination; and
  - (iii) incorporation of the substituted total annual revenue amount in the *pricing proposal* under clause 8A.14.4(~~fd~~),such variations will be taken to be explained by the relevant NSW DNSP for the purposes of clause 6.18.8(a)(2);
- (3) if clause 8A.14.4 applies, the reference to 'any applicable distribution determination' in clauses 6.18.2(b)(7), 6.18.2(b)(8), 6.18.8(a)(1) and 6.18.8(c) will be taken to be the applicable distribution determination as supplemented by the requirements for the NSW DNSP's *pricing proposal* under clause 8A.14.4(~~fd~~);
- (4) to the extent that a NSW DNSP's tariffs vary from tariffs which would result from complying with the pricing principles in clause 6.18.5(e) to (g) due to the application of this *participant derogation*, such variation is taken to be a variation from the pricing principles permitted under clause 6.18.5(c);
- (5) clause 6.18.6 does not apply to the extent that a NSW DNSP's tariffs vary from tariffs which would otherwise result from complying with clause 6.18.6, due to the application of this *participant derogation*; and
- (6) if the AER amends a *pricing proposal* under clause 6.18.8(b)(2) or 6.18.8(c), then in addition to the requirements in clause 6.18.8(c1), the AER must also have regard to:
  - (i) if ~~clause~~ 8A.14.4(a)(1) applies, any variation in proposed tariffs as a result of the remade 2015 determination;

- (ii) if clause 8A.14.4(a)(2) applies, any variation in proposed tariffs as a result of the affirmed or varied 2015 determination (as the case may be); and
  - (iii) if the *AER* determines an adjustment amount and subsequent adjustment under clause 8A.14.4(b), any variations in proposed tariffs as a result of the application of the substituted total annual revenue amount under clause 8A.14.4(~~df~~).
- (c) For the purposes of the application of clauses 8A.14.4, 8A.14.5 and 8A.14.6 (as applicable) in respect of a NSW DNSP, Chapter 6 is amended for the subsequent regulatory control period as follows:
- (1) if clause 8A.14.6 applies, clause 6.5.9(b)(2) does not apply to the extent necessary to include the adjustment amount or subsequent adjustment amount (as applicable) as a revenue increment or revenue decrement (as the case may be) to the *annual revenue requirement* of one or more regulatory years for the subsequent regulatory control period for the relevant NSW DNSP under clause 8A.14.6(c); and
  - (2) the reference to ‘the other revenue increments or decrements’ referred to in clauses 6.4.3(a)(6) and 6.4.3(b)(6) is taken to include such increments or decrements as adjusted to the extent necessary to take into account the application of the substituted total annual revenue amount under clause 8A.14.4(d).
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## Attachment 3: Explanation of proposed alternate wordings

| Proposed changes   | Proposed alternate wording  | Explanation  |
|--|---|--|
| <p><b>Calculation of revenue amount adjustment – propose to use only one term ‘adjustment amount’<sup>5</sup>.</b></p> | <p><b>adjustment amount</b> in respect of a NSW DNSP, means an amount equivalent in net present value terms to the difference between:</p> <ul style="list-style-type: none"> <li>(a) the current allowed revenue; and</li> <li>(b) the current actual revenue,</li> </ul> <p>at the regulatory year in which the adjustment determination is made, provided that:</p> <ul style="list-style-type: none"> <li>(c) if the adjustment amount is positive, it will be a revenue increment; and</li> <li>(d) if the adjustment amount is negative, it will be a revenue decrement.</li> </ul> <p><b>current allowed revenue</b> means the sum of:</p> <ul style="list-style-type: none"> <li>a) the annual revenue requirements approved by the AER in the remade 2015 determination for each previous or current regulatory year of the current regulatory control period, and</li> <li>b) adjustments required to effect the application of the control mechanism formulae in each relevant year of the current regulatory control period.</li> </ul> <p><b>current actual revenue</b> means the sum of</p> | <p>It should be noted that Ausgrid’s proposed ‘adjustment amount’ term replaces the ‘variation amount’ in the Rule as currently drafted. This is because under our proposed alternative drafting, only one operative term is needed.</p> <p><b><u>Adjustment amount</u></b></p> <p>The function of the ‘adjustment amount’ is to give effect (in a clear and transparent way) to the objective that NSW DNSPs should not be able to recover more (or be deprived of more) revenue that they are entitled to under the AER’s remade determination or affirmed/varied determination. This is done by defining this amount as the difference between the revenue the DNSPs are entitled to and the actual amounts recovered or expect to be recovered to date.</p> <p>Looking at the issue a different way, this calculation is analogous to the calculation of the overs/under accounts balance which is predicated on the same concept. That is, the control mechanism imposed by the AER is that of a revenue cap and the NSW DNSPs should not be allowed to earn revenue above that cap. Consequently any over- recovery is to be returned from customers and any under-recovery is to be recovered from customer in future years. The same concept underpins the definition of ‘adjustment amount’ that we have proposed.</p> <p><b><u>Current allowed revenue</u></b></p> <p>This definition:</p> |

<sup>5</sup> Instead of an additional term ‘variation amount’.

| Proposed changes | Proposed alternate wording  | Explanation   |
|------------------|---|---|
|                  | <p>revenue actually earned or expected to be earned, or the revenue used in the setting of transmission use of system charges by TransGrid (if applicable) in each previous and current regulatory year of the current regulatory control period.</p> | <p>a) Refers to the new annual revenue requirement that the DNSPs are entitled to earn under a remade 2015 determination. That is, this is the revenue the NSW DNSPs would have been entitled to recover if the remade determination was in place as at the beginning of the regulatory control period. We consider that this revenue amount encompasses the annual update to the cost of debt which would have occurred as a matter of course.</p> <p>b) Includes revenue amounts from:</p> <p>a. The application of the control mechanism formulae imposed by the AER. This is to ensure that any revenue amounts that would have been included in the total revenue in the annual pricing proposal would be included. In Ausgrid's case, these are:</p> <p>i. 'B-factor revenue' which encompasses approved pass through amounts for the April 2015 storm, adjustment for GoEnergy Retailer insolvency and any D-factor adjustment.</p> <p>ii. 'S-factor financial reward / penalty' from the application of the STPIS. We consider that the calculation of the financial penalty/reward for the STIPIS should be made based on the final approved/revenue amounts for the 2014-19 period as set out in the AER's remade determination.</p> <p><b><u>Current actual revenue</u></b></p> <p>This definition:</p> <p>a) Refers to the actual revenue recovered for each year of the 2014-19 regulatory period or the revenue expected to be earned if actual is not yet available (for example FY 2019).</p> |

| Proposed changes  | Proposed alternate wording   | Explanation  |
|---|--|--|
|   |  | <p>b) with respect to Ausgrid's revenue from dual function assets, it is the revenue provided to TransGrid for setting transmission use of system charges for each year of the 2014-19 period.</p>   |
| <p><b>Principle to be applied when determining the adjustment amount.</b></p> | <p>Additional subclause (c) to follow subclause (b) and renumber existing clause (c) and (d). This adopts the AER's suggested approach with some minor wording adjustments.</p> <p><b>(c)</b> When determining an adjustment amount the AER must be satisfied that the adjustment determination will result in the relevant NSW DNSP's allowed revenue being the same (in net present value terms) as it would have been if the remade 2015 determination had been in place from the commencement of the current regulatory period and the control mechanism and control mechanism formulae specified in the remade 2015 determination had applied in each relevant regulatory year.</p> | <p>This new clause (c) together with existing subclause (b) requires the AER to take the first step in a two-step process, i.e. determine the total adjustment amount being an amount that will result in the NSW DNSP have the same allowed revenue as it would have recovered if the remade determination had been in place from the beginning of the regulatory control period and the control mechanism and control mechanism formula had been applied.</p>  |
| <p><b>Allocation of adjustment amount between regulatory periods</b></p>      | <p>Clause 8A.14.4(c) of Ausgrid's proposed alternate Rule requires the AER to allocate amounts between the current period and subsequent period, subject to the principles set out under paragraph (d).</p> <p><b>Current adjustment amount</b>, in respect of a NSW DNSP, means that proportion of the adjustment amount determined by the AER to apply in the current regulatory control period under clause 8A.14.4(c).</p> <p><b>Subsequent adjustment amount</b>, in respect of a</p>   | <p>These definitions have been proposed to give effect to the second step of the process which is concerned with the recovery of the adjustment amount, i.e. the allocation of the adjustment amount between regulatory periods under scenario 1. For scenarios 2 and 3, the whole adjustment amount (in NPV equivalent terms) is allocated to the subsequent period.</p> <p><b><u>Current adjustment amount</u></b></p> <p>This is the portion of the adjustment amount that the AER has determined, subject to certain principles which are outlined below, should be recovered in the last year of the 2014-19 period. This adjustment amount is to be added to / deducted from the revenue</p> |

| Proposed changes | Proposed alternate wording  | Explanation  |
|------------------|---|--|
|                  | <p>NSW DNSP, means an amount that is equivalent in net present value terms to the amount that is equal to the adjustment amount less the current adjustment amount.</p> | <p>allowed to be recovered in the final year via the pricing proposal (termed 'substituted total annual revenue amount').</p> <p><b><u>Subsequent adjustment amount</u></b></p> <p>This is the amount to be included in the building block revenue for the 2019-24 period. Under scenario 1, this amount reflects the difference between the adjustment amount and the current adjustment amount (in NPV equivalent terms). In scenarios 2 and 3, this amount is equivalent in net present value terms to the adjustment amount.</p> <p>There are a couple of matters to note in relation to the subsequent adjustment amount:</p> <ul style="list-style-type: none"> <li>• The definition refers to an equivalent amount in net present value terms. In ensuring NPV neutrality, we consider that this should be done using the discount rate determined by the AER for the 2014-19 period (under either a remade decision or affirmed/varied decision) and not of the subsequent period. This is to ensure that the DNSP is 'made whole' as if a valid determination of the 2014-19 period was in place on 1 July 2014.</li> <li>• The subsequent adjustment amount will need to be excluded when applying the incentive schemes determined by the AER to be applicable for the 2019-24 period. This is to ensure that the financial outcomes of applying incentive schemes in 2019-24 period are based on the revenue for that period only and are not based on revenue amounts inclusive of the revenue of the prior period. For example, in calculating the financial penalty / reward under the STPIS for the 2019-24 period, the subsequent adjustment amount included in the building block revenue for 2019-24 is to be excluded. This exclusion applies under all scenarios 1, 2 and 3.</li> </ul> |

| Proposed changes  | Proposed alternate wording   | Explanation   |
|---|--|---|
| <p><b>Principles to be taken into account in allocation of revenue between periods.</b></p> | <p>Clause 8A.14.4(d) has been altered to set out the principles that Ausgrid considers the AER needs to take into account in allocating the adjustment amount between periods. These principles are:</p> <ol style="list-style-type: none"> <li>1. Reasonably likely to minimise prices variations between years and periods.</li> <li>2. Will provide the DNSPs with an opportunity to fully recover the revenue allowed by the AER.</li> </ol> | <p>We have amended this clause to include an additional principle that we consider the AER needs to take into account in allocating the adjustment amounts between periods, in addition to the over-arching objective of minimising price variations. This principle is that the AER’s decision in choosing the smoothing profile to allocate revenue between periods, such that price volatility is minimised, should provide the DNSP an opportunity to fully recover the revenue that it is entitled to.</p> <p>If there is a smoothing profile that achieves the over-arching objective and allow the DNSP the opportunity to fully recover its revenue entitlement, then the AER should choose that profile instead of one that, while allowing for price minimisation, does not allow the DNSPs an opportunity to fully recover its revenue entitlements. This principle is to recognise that there may be constraints on the DNSPs to fully recover the revenue path set by the AER for a particular year.</p> |
| <p><b>Other adjustments</b></p>   | <ul style="list-style-type: none"> <li>• Other clauses of the draft Rule have been deleted, amended or added as a consequence of amending the definition of ‘adjustment amount’ and/or inclusion of ‘current adjustment amount’ and ‘subsequent adjustment amount’.</li> <li>• Correcting the definition of Ausgrid and Endeavour Energy.</li> </ul>   | <ul style="list-style-type: none"> <li>• For example, the term ‘variation amount’ and ‘total annual revenue’ have been deleted as they are redundant.</li> <li>• The term ‘scheme’ has been added to specify the various incentive schemes.</li> </ul>  |