

14 March 2013

Mr John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Dear Mr Pierce

RE: NSW DNSPs' Response to Consultation Paper - *National Electricity Amendment (Changes to cost allocation method) Rule 2013* (Reference ERC0150)

The NSW Distribution Network Service Providers, Ausgrid, Endeavour Energy and Essential Energy (the NSW DNSPs) welcome the opportunity to provide this joint submission to Trans Tasman Energy Group's (TTEG's) Rule change proposal.

It is our understanding that TTEG is seeking to amend provisions of the National Electricity Rules (Rules or NER) to address problems it has experienced when attempting to negotiate the terms and conditions for the provision of negotiated services. Whilst the proponent has not articulated or demonstrated how these problems have arisen in practical terms, it appears that it has experienced the following issues:

- A lack of transparency in how prices for negotiated services are established;
- An inability to engage effectively in negotiation; and
- Concerns that the price established for negotiated service may not be cost reflective (i.e. that prices may be inflated) and/or not NER compliant.

The NSW DNSPs note that the issues identified by TTEG's Rule change request primarily relate to issues surrounding the negotiation of negotiated distribution services (negotiated services). While the NSW DNSPs have not been requested to provide negotiated services during the current regulatory control period, we understand the framework for these services and understand that they are provided in accordance with the negotiating framework and negotiated distribution service criteria (NDSC) as determined by the Australian Energy Regulator (AER) as part of each DNSP regulatory determination.

If a service applicant is concerned that a network service provider is not complying with its obligations or that it is being overcharged, it can raise a dispute to the AER under Part L of the Rules.

The Rule change request to establish the content of a DNSP's cost allocation method (CAM) fails to demonstrate how existing mechanisms are unable to address TTEG's concerns. As not every DNSP has negotiated services, amending the CAM to address a deficiency with the negotiating framework is not an appropriate solution and has far reaching impacts beyond the price established for negotiated services.

Without further information on the specific problems TTEG is experiencing, we find it difficult to understand how TTEG's issues cannot be resolved by the mechanisms outlined above. Consequently, while the NSW DNSPs would support improvements to address demonstrated deficiencies in the negotiated framework, we do not support the proposed changes.

These matters are addressed in further detail in the attached submission, which also contains our response to the questions raised in the AEMC's consultation paper.

If you have any queries or wish to discuss further please contact Mike Martinson, Group Manager Regulation at Networks NSW on (02) 9853 4375 or via email at michael.martinson@endeavourenergy.com.au

Yours sincerely,



Vince Graham
Chief Executive Officer
Ausgrid, Endeavour Energy and Essential Energy

Attachments

1. NSW DNSPs' Response (Reference ERC0150)

Attachment: NSW DNSPs' Response (Reference ERC0150)***Appropriate mechanisms already address Trans Tasman Energy Group's concerns***

The NSW DNSPs note that the issues identified by Trans Tasman Energy Group's (TTEG's) rule change request primarily relate to issues surrounding the negotiation of negotiated distribution services (negotiated services).

While the NSW DNSPs have not been requested to provide negotiated services during the current regulatory control period, we understand the framework for these services and understand that they are provided in accordance with the negotiating framework¹ and negotiated distribution service criteria (NDSC).²

The framework for negotiated services contains a number of mechanisms to ensure that service applicants are able to effectively engage in the negotiation of negotiated services. We have outlined these mechanisms below in Table 1, and have also sought to demonstrate how these mechanisms address TTEG's concerns.

Table 1 – Existing mechanisms that address *Trans Tasman Energy Group's* concerns

Issue raised by the TTEG	Mechanism that addresses TTEG's concern	Description of how mechanism addresses TTEG's concern
Inability for stakeholder's to engage effectively in negotiations for negotiated services	The negotiating framework and NDSC are open to public consultation	Both the NDSC and negotiating framework are determined by the AER as part of each DNSP's regulatory determination. Stakeholders are able to engage with both the regulator and the DNSP on how negotiations for negotiated services should be undertaken. Through this forum stakeholders are able to raise concerns regarding a DNSP's negotiating framework and can suggest ways in which the framework can be amended to facilitate consumer engagement or achieve better outcomes.
	Clause 6.7.5 (c)(1) and clause 6.7.5 (c)(4) of the National Electricity Rules (NER).	Under the negotiating framework, DNSPs are required to negotiate in good faith and provide all commercial information reasonably required to enable a service applicant to engage effectively in negotiations.
Lack of transparency regarding how DNSP's establish prices for negotiated services	Clause 6.7.4 (1) (application of NDSC)	The AER determines the NDSC that is to apply to negotiated services, as part of the DNSP's regulatory determination. The DNSP must apply the NDSC in establishing access charges and the price for the provision of a negotiated service.
	Clause 6.7.5(3) of the NER.	DNSP's are required to: <ul style="list-style-type: none"> • identify the reasonable costs of providing the negotiated distribution service; • demonstrate to the service applicant that the charges for the negotiated distribution services reflect those costs; and • have appropriate arrangements for assessment and review of the charges and the basis on which they are made.
Prices charged by DNSP's negotiated services are inflated and/or not compliant with the NER	Clause 6.7.5(c)(6) and 6.22 of the NER (dispute resolution process)	If a service applicant is concerned that a DNSP is not complying with its obligations under the negotiating framework, it is able to raise a dispute to the AER. Therefore, if a service applicant was concerned that the price for a negotiated service was not cost reflective, or that the DNSP had not provided commercial information to enable it to negotiate effectively, the applicant is able to refer these matters to the AER.

It is not clear from the proposal whether TTEG has indeed utilised these NER review processes to obtain the confidence in the processes and negotiation outcomes that it appears to be seeking. As a general principle all oversight and review mechanisms should be exhausted before seeking to change the NER. Indeed it is our understanding that the review mechanisms currently in place in the NER to support the processes of negotiating services were included to, in part, address the general theme of concerns expressed by TTEG in its Rule change proposal.

¹ The negotiating framework sets out the procedure to be followed during negotiations between a DNSP and any person wishing to receive a negotiated distribution service.

² The negotiated distribution service criteria (NDSC) sets out the criteria that DNSPs are to apply in negotiating terms and conditions (including price) of access for negotiated services. The NDSC is also applied by the AER in resolving disputes regarding these terms and conditions. See clauses 6.7.2, 6.7.4 and 6.22.2(c) of the NER.

Consequently, while the NSW DNSPs would support improvements to address demonstrated deficiencies in the negotiated framework, we do not support the proposed changes.

Without further information on the specific problems TTEG is experiencing, we find it difficult to understand how TTEG's issues cannot be resolved by the mechanisms outlined above. The Rule change request fails to demonstrate how existing mechanisms are unable to address TTEG's perceived concerns. Consequently, the NSW DNSPs consider that TTEG has not substantiated the need for a Rule change.

Other solutions better address the concerns raised by Trans Tasman Energy Group

The NSW DNSPs do not support TTEG's proposal to mandate numeric quantities for each cost allocator contained in a DNSP's cost allocation method (CAM). The NSW DNSPs consider that this requirement is too prescriptive, is not an effective means for achieving the outcome that TTEG is seeking and duplicates existing obligations.

Moreover, in many instances *ex ante* numeric quantities for each allocator will not always be consistent with the Rule requirements to ensure that costs are allocated on a causal basis noting that the causal allocator quantities will only be known with certainty *ex post*.

TTEG has argued that prescribing the CAM is necessary in order for service applicants to³:

- Engage effectively in negotiation for the price of negotiated services;
- Identify and inform the service applicant of the reasonable costs of providing the negotiated service; and
- To ensure that negotiated services are provided on a 'cost reflective' basis.

While the NSW DNSPs do not have any recent experience with the provision of negotiated services, we assume that a service applicant is able to engage effectively in negotiations if the DNSP has complied with its obligations to provide the applicant with all commercial information reasonably required to enable the applicant to engage effectively in negotiations.⁴

Further, the NSW DNSPs do not see how providing a numeric quantity for how costs are allocated will enable service applicants to engage more effectively in negotiations. The CAM sets out the basis for how a DNSP allocates its costs to various services, and while the NDSC and the negotiating framework require prices for negotiated services to be cost reflective, the CAM determines how costs are allocated.

It is critical to recognise that the CAM is required to address the allocation or attribution of a range of costs with differing relationships to a specific service or groups of services. Specifically, the cost allocation guideline defines a hierarchical approach to cost allocation based on these relationships such that:

- Where costs are directly related to a service they should be directly attributed to that service;
- Where they cannot be directly attributed to a single service they should be allocated on a causal basis; and
- Where a relationship cannot be readily identified without undue cost the costs should be allocated to services using a reasonable allocator.

As a general rule, the experience with cost allocation arrangements for the NSW DNSPs is that more costs are directly attributed (i.e. not allocated) than are allocated on a non-causal basis. In other words, the costs of services are generally derived from the direct and identifiable costs of the specific service which we believe would be relatively transparent. Consequently, the CAM's ability to influence the price of negotiated services or a service applicant's ability to negotiate effectively due to "non-transparent" cost allocation appears limited.

³ Trans Tasman Energy Group, Proposed Rule Change, 7 December 2012, pp3 and 6.

⁴ See clause 6.7.5(c)(2) of the NER.

Amending the CAM would duplicate existing requirements as the negotiating framework already contains mechanisms that require prices to be established on a cost reflective basis.⁵ If a service applicant is not satisfied that a DNSP has complied with this obligation, it is able to raise a dispute with the AER, which has the appropriate information gathering powers to execute this function. Moreover, from a policy perspective it would appear inappropriate to impose the obligation to ensure compliance with the CAM to parties involved in a negotiation as this would impose an inappropriate level of costs and burden on parties seeking to negotiate costs that could create an economic barrier to fair negotiations.

Further, if there is a deficiency in the operation of these mechanisms then a more appropriate solution would be to strengthen these arrangements rather than amend the CAM. The NSW DNSPs consider that this offers a more targeted and effective approach for addressing TTEG's concerns.

The negotiating framework and NDSC govern how negotiation is conducted and prices for services are established; whereas the CAM is a much broader instrument aimed at determining how costs are allocated to various services.

Prescribing the CAM may have unintended consequences

The NSW DNSPs consider that TTEG's proposal to amend the CAM so that DNSP's are required to provide a numeric quantity for each allocator, regardless of whether the allocator is likely to change, is overly prescriptive and undermines the efficiency of the CAM.

The NSW DNSPs are concerned that this proposed amendment will have a number of unintended consequences. Specifically, that it will result in:

- Inefficient allocation of resources;
- Increased regulatory burden and compliance costs for DNSPs; and
- Price impacts to consumers.⁶

The provisions in the NER regarding the CAM are based on high level principles and policies rather than prescriptive clauses. The AER Cost Allocation Guidelines (CAG) set out the detailed requirements that DNSPs must comply with in preparing a compliant CAM and are intended to give effect to the cost allocation principles in the NER.

Enshrining the high level cost allocation principles in the NER and placing the detailed requirements in guidelines allows the provisions for establishing the content of DNSP's CAM to operate flexibly and effectively.⁷ Having a principle based approach also means that the CAM does not require frequent updating.

The current approach for establishing the content of DNSP's CAM provides DNSPs with the flexibility to tailor their CAM to reflect their individual circumstances. Under the current approach, DNSPs are able to determine the most appropriate method for allocating costs to a particular service taking into account the casual relationship between the cost driver(s) and cost category, as well as the effort and costs involved in applying the cost allocator.⁸

Currently, in submitting a proposed CAM, DNSPs must detail whether or not a cost allocator is likely to remain unchanged during the course of the regulatory period. Only when an allocator is likely to remain unchanged, is a numeric quantity or percentage for the allocator to be included in the CAM.

For some DNSPs, the most appropriate allocation basis for a cost category may be to use a methodology that contains a numeric quantity, as this approach best reflects the cost driver for providing the service and is unlikely to change during the regulatory control period. However, for other DNSPs the numeric quantity of a cost driver for a particular cost category fluctuates annually. Under these circumstances, the DNSP would outline the cost allocation basis in its CAM for the applicable

⁵ DNSP's are required to inform the service applicant of the relevant cost of providing a negotiated service, demonstrate that these costs are cost reflective and must provide arrangements to have these costs and their basis assessed. See clause 6.7.5(3) of the NER.

⁶ Imposing onerous regulatory obligations will increase DNSP's compliance costs, which will ultimately be passed through to consumers in the form of higher electricity prices.

⁷ Currently, a DNSP's approved CAM is amended on an ad hoc basis when it becomes apparent there is a more appropriate method for allocating a particular cost. As the focus of the CAM is on the methodology for assigning costs, as opposed to the detailed quantity of each cost driver, it is able to remain relevant for long periods of time.

⁸ Clause 6.15.2(3)(ii) of the NER.

cost category but would not disclose a numeric quantity. This is because disclosing such a quantity would result in undue cost and effort from DNSPs having to frequently amend the CAM to reflect the change in numeric quantities and for the AER to frequently review such changes.

For example, Ausgrid allocates the costs for its business technology services on the basis of full time employee splits (FTEs). Ausgrid allocates its costs in this manner due to the strong causality between the number of staff and the need and use of business technology services by Ausgrid personnel.⁹ Ausgrid's CAM does not include a numeric quantity for this cost allocator as the number of FTEs can fluctuate from year to year.

Therefore, TTEG's proposed amendment to require DNSPs to disclose numeric quantities for each of its cost allocators, regardless of whether the numeric quantities (or underlying data) of a cost allocator are likely to change during the regulatory control period, will result in some DNSPs having to apply more frequently to the AER to have their CAM amended.

For the NSW DNSPs, this requirement may mean that we will have to submit a CAM to the AER on a yearly basis, as opposed to as required by the business.¹⁰ We consider that this undermines the effectiveness and flexibility of existing CAM provisions and would create a significant regulatory burden for businesses and the AER alike.

Further, this may result in an inefficient allocation of resources for DNSPs and the AER, particularly if the approval process was subject to public consultation.

DNSPs would need to devote more time and resources in preparing a compliant CAM and would need to do so more frequently. For instance, it takes approximately two to three months for a DNSP to prepare a compliant CAM for AER approval and six months for the AER to make a determination. If the CAM had to be amended on a yearly basis this would mean that CAMs would effectively be in a continuous review and change phase with DNSPs having to undertake work to update their CAM three months after the AER had approved the CAM.

Moreover, the potential for frequent or annual updating of each business's CAM is likely to create challenges for ensuring that the information being reported to the AER annually is comparable over time which may raise concerns (real or perceived) as to the use of the information for benchmarking and revenue reset purposes.

Consequently, the NSW DNSPs are concerned that the proposed changes will result in higher electricity prices for consumers with little perceivable benefit. This is because the increased costs associated with complying with the proposed amendments will ultimately be passed through to consumers in the form of higher electricity prices. Given that not every DNSP has negotiated services, amending the CAM to address a deficiency in the negotiating framework imposes additional costs to all consumers, most of whom will not receive any benefit from having greater transparency regarding how DNSPs allocate their costs to various services.

Mechanisms already exist that require DNSPs to comply with their CAM

The NSW DNSPs understand that an underlying driver of TTEG's Rule change request is to ensure that prices for negotiated services are cost reflective and NER compliant. As noted in Table 1, there are a number of mechanisms that seek to achieve this aim. Further, mechanisms already exist that require compliance with the CAM. These include:

- Annual regulatory accounts - DNSPs must demonstrate compliance with their CAM in preparing their annual regulatory accounts.¹¹ Before submitting regulatory accounts to the AER, they must be signed off by the DNSP's Board and also audited by an external body.
- Cost Allocation Method Guideline - The AER is able to request a DNSP to demonstrate its compliance with its CAM.¹² The AER is also able to request a review of a DNSP's financial

⁹ Ibid, p 9. In accordance with clause 6.15.2(3)(ii) shared costs incurred in providing several categories of distribution services must be allocated between those services using an appropriate causal allocator.

¹⁰ A DNSP may seek to have its CAM amended to reflect a more appropriate basis for allocating costs to a particular cost category.

¹¹ DNSPs must submit audited regulatory accounts to the AER as part of their annual information requirements. The auditors are required to comply with the directions set out by the AER in respect of issues to be reviewed including a detailed review of the application of the CAM.

¹² AER Electricity distribution network service providers cost allocation guidelines, June 2008, clause 5.2(b). If requested, a DNSP must submit a supporting paper demonstrating how it has applied the detailed principles and policies in its approved

information and may specify CAM assurance requirements that will be placed in future regulatory information instruments.¹³

- Regulatory Revenue Proposal – In preparing their regulatory revenue proposals DNSPs must submit evidence demonstrating that their forecasted expenditure complies with their approved CAM.¹⁴

Conclusion

Not every DNSP has negotiated services. Therefore to amend the CAM to address a deficiency with the negotiating framework is not an appropriate solution and has far reaching impacts beyond the price established for negotiated services.

While the NSW DNSPs support the principles of transparency and consumer engagement we do not support TTEG's proposed amendments to the Rules for the following reasons:

- the Rule change request fails to substantiate the need for a Rule change;
- the proposed amendments do not provide an effective solution to the issues identified in the Rule change request; and
- prescribing the CAM in the manner proposed by TTEG is inappropriate, unnecessary and may give rise to a number of unintended consequences.

Consequently, the NSW DNSPs do not support TTEG's proposed Rule change and consider that the Rule change does not contribute to the achievement of the National Electricity Objective.

CAM; outline the numeric quantity or percentage of the allocator or allocators applied to each cost item; and explain how the numeric quantity or percentage of each allocator has been calculated for each cost item, including where the data for determining the numeric quantity or percentage has been sourced.

¹³ Ibid, clause 5.3(a).

¹⁴ See clause 6.5.6(b)(2) and clause 6.5.7(b)(2) of the NER.

NSW DNSPs' Response to AEMC Questions

Question 1

Is the assessment framework presented in this consultation paper appropriate for assessing this rule change request?

No comment.

Question 2

How often is the cost allocation method likely to change? What are the costs for stakeholders, including the AER, of public consultation for a change in the cost allocation method?

The cost allocation method (CAM) is based on high level principles and policies. Once approved by the AER, a CAM remains current until a DNSP determines that a more appropriate allocation basis exists for a particular cost category or the AER requests a change to take into account any change to the Cost Allocation Guidelines. Consequently, approved CAMs tend to be amended by a DNSP from time-to-time as required by the business or the AER.

Currently, when preparing a CAM for the AER's approval, a DNSP must detail whether or not a cost allocator is likely to remain unchanged during the course of the regulatory period. Only where an allocator is likely to remain unchanged, is a numeric quantity or percentage for the allocator should be included in the CAM.¹⁵

The current cost allocation guidelines provide DNSP's with the flexibility to tailor their CAM to suite their individual circumstances. For some DNSP's, the most appropriate allocator for a cost category may be to use a methodology that contains a numeric quantity, as the quantity best reflects the cost driver for providing the service and is unlikely to change during the regulatory control period.

However, for other DNSPs, the numeric quantity of a cost driver for a particular cost category fluctuates annually. Under these circumstances, the DNSP would outline the cost method in its CAM for the applicable cost category but would not disclose a numeric quantity. This is because disclosing such a quantity would result in undue cost and effort from having to frequently amend the CAM to reflect the change in numeric quantities.

For example, Ausgrid's IT costs are allocated between standard control, alternative control and unregulated services based on full time employee (FTE) splits. This reflects the strong casual link between the number of staff and the need and use of IT infrastructure. If Ausgrid were to provide a percentage for its FTE splits between each services it would need to amend its CAM throughout the regulatory control period to reflect fluctuations in the level of FTEs.

Consequently, as the CAM is based on high level principles and policies it is able to be applied flexibly and remain relevant for long periods of time. Prescribing the CAM so that DNSPs are required to provide numeric values for each cost allocator regardless of whether the numeric value is likely to remain unchanged, undermines the efficiency of the CAM.

Imposing such a requirement may result in some DNSPs having to amend their CAM on a yearly basis. This may amount to a significant diversion of resources for DNSPs and the AER. This is because it takes DNSP's approximately two to three months to prepare their CAM for AER approval, with the AER having six months to make its determination. If this task had to be undertaken on a yearly basis to reflect changes to numeric values of cost allocators (as opposed to as required) some DNSP's would have an approved CAM for three months before having to repeat this process all over again.

The associated costs from prescribing the CAM and having public consultation would be time and resources for DNSPs and the AER, with the magnitude of these costs being dependant on the frequency that the CAM would need to be amended to be NER compliant.

DNSPs would incur costs from having to comply with this obligation as they would need to allocate time and resources to track their ongoing compliance with the CAM, prepare amendments to the CAM more frequently, and make corresponding changes to financial and

¹⁵ AER Electricity distribution network service provider cost allocation guidelines, June 2008, p 8.

accounting systems to account for the change in numeric value. This would constitute a diversion of resources and time from the DNSP's business as usual activities.

Similarly, the AER would also need to dedicate resources to assessing DNSPs' CAMs on a more frequent basis, where these resources would otherwise have been dedicated to other monitoring and enforcement functions.

Question 3

What information is included in the cost allocation method in practice? How does this differ between DNSPs? Is comparability of cost allocation methods between DNSPs relevant to the negotiation framework? What is the cost of providing more detailed information of allocators?

The NER outlines the high level cost allocation principles which are to be reflected in every DNSP's CAM.¹⁶ The AER's Cost Allocation Guidelines are designed to give effect to the cost allocation principles and sets out the detailed requirements that the DNSP must comply with in submitting their CAM for approval.

Consequently, it is the AER's Cost Allocation Guideline which determines the information that is to be included by DNSPs in submitting their CAM to the AER for approval. Under the current Cost Allocation Guidelines DNSPs are required to include information on¹⁷:

- The nature of each cost item;
- The category or categories of distribution services to which the cost item is to be allocated;
- The characteristics of the cost item that associate it uniquely with a particular category of distribution service in order to make it a directly attributable cost;
- How and where records will be maintained to enable the basis of attribution to be audited or otherwise verified by a third party;
- The nature of the allocator, or allocators to be used for allocating each cost item for shared costs;
- The reason for selecting the allocator, or allocators, for each cost item and an explanation of why it is the most appropriate available allocator, or set of allocators for each cost item;
- Whether the numeric quantity or percentage of the allocator or allocators to be applied for each cost item will (i) remain unchanged over the regulatory control period¹⁸ or (ii) change from time to time throughout the regulatory control period;¹⁹
- The version, history and date of issue of the DNSP's proposed CAM;
- A statement of the nature, scope and purpose of the document and the way in which it is to be used by the DNSP;
- Details of the accountabilities within the DNSP for implementing the CAM;
- responsibilities within the DNSP for updating, maintaining and applying the CAM and for internally monitoring and reporting its application;
- A description of the DNSP's corporate and operational structure to enable the AER to understand how the DNSP is organised to provide its distribution services; and
- A specification of the categories of distribution services that the DNSP provides to which costs are to be attributed or allocated and the types of persons to whom those services are to be provided.

The NSW DNSPs do not see how comparability of CAMs between DNSPs is relevant to the provision of negotiated services. Each DNSP's CAM will differ due to historical differences

¹⁶ See clause 6.15.2 of the NER.

¹⁷ AER Electricity distribution network service providers – Cost allocation guidelines, June 2008, clause 2.2 and 3.2.

¹⁸ Ibid, clause 2.2.1(b)(F) requires a DNSP to provide that details of the numeric quantity or percentage of the allocator or allocators and an explanation of how the numeric quantity or percentage has been calculated, including where the data for determining the numeric quantities or percentages are to be sourced.

¹⁹ Ibid, clause 2.2.1(b)(G) requires the DNSP to provide an explanation of how the DNSP intends to calculate the numeric quantity or percentage throughout the regulatory control period, including where the data for determining the changing numeric quantities or percentages are to be sourced.

between DNSPs and the nature of each individual DNSPs network, as well as different cost drivers. Each DNSP allocates its cost for providing a particular service according to the most appropriate allocator for a given cost category.

Further, the price established for a negotiated service will depend on the circumstances surrounding the provision of the service (i.e. the specific nature of the service to be provided, access requirements and whether additional work is necessary for safety or reliability reasons) rather than the methodology used by a DNSP for allocating costs to negotiated services.

As noted in question 2, the associated costs from providing more information is time and resources. The magnitude of these costs will differ for DNSPs depending on the how frequently they will need to update their CAMs in order to provide numeric quantities for their cost allocators. For DNSPs that will have to amend their CAMs on a yearly basis to meet this requirement the cost could be quite significant.

Question 4

Are the problems that the proponent identified also present in the transmission frameworks for cost allocation method and negotiated services?

The NSW DNSPs consider that this issue would be more relevant to transmissions networks given that they tend to provide more negotiated services.

Question 5

Is additional consultation required? Are the Distribution Consultation Procedures an appropriate framework for consultation in this context? Will the AER have sufficient time to adequately consider stakeholder views with the consultation procedures? Will consultation delay changes to a cost allocation method?

NSW DNSPs support the principle of transparency; however, we consider that it is important to weigh the benefit of consultation against its associated costs.

We note that stakeholders are already able to provide input into DNSP's CAM by providing feedback and comments on the AER's Cost Allocation Guidelines. The NSW DNSPs consider that this provides an optimal avenue for public consultation, as the AER's guidelines determines how each DNSP is required to develop its CAM. Consequently, we consider that it would be more efficient if DNSP's CAM was not subject to the distribution consultation procedures.

Whether applying the distribution consultation procedures to each DNSP's CAM will cause delay is matter for the AER to provide comment on.

Question 6

Will the inclusion of numeric quantities require more frequent updating of cost allocation methods? Does the proposed solution to include numeric quantities achieve the aim of including sufficient information to replicate costs to be recovered?

The NSW DNSPs believe that the inclusion of numeric quantities will require more frequent updating of our CAM and consider that this requirement would be difficult to implement.

For some DNSPs this requirement may mean that their CAM will need to be amended on a yearly basis, as opposed to as required by the business or the AER. This would prove impractical as a DNSP will not actually know what the numeric quantity will be from year to year until well after the end of the financial year. The DNSP would then have to prepare a revised CAM for approval by the AER before it could commence preparation of annual regulatory accounts, and it would be highly unlikely for the CAM to be approved before the annual regulatory accounts were due. Under this scenario, demonstrating compliance with the approved CAM when submitting annual regulatory accounts would be impossible to achieve.

The NSW DNSPs strongly argue that prescribing the CAM so that numeric quantities or percentages are required for each cost allocator is unnecessary and inappropriate. We consider this to be a very convoluted way for determining whether the price established for a negotiated service is cost reflective. As noted in our submission, if a service applicant is not

satisfied that the price established for a negotiated service is cost reflective it can raise a dispute to the AER, under Part L of the NER.

Further, there are already a number of mechanisms that require a DNSP to demonstrate its compliance with its CAM such as when it submits its regulatory accounts and its regulatory determination.²⁰ In addition, the AER is also able to request a DNSP to demonstrate its compliance with its CAM.²¹

The NSW DNSPs consider that mechanisms already exist to ensure that prices for negotiated services are cost reflective and further that DNSP's comply with their CAM. We believe that prescribing the CAM to achieve this outcome is inappropriate and does not contribute to the achievement of the NEO. The associated transparency benefits from requiring DNSP's to provide numeric quantities are far outweighed by the associated costs of:

- Increased regulatory burden and compliance costs for DNSPs;
- Inefficient allocation of resources;²² and
- price impacts to consumers²³

See also the NSW DNSPs response to questions 2.

Question 7

To what extent do the existing principles influence the negotiation criteria? Is imposing a pricing requirement consistent with the level of regulation appropriate for negotiated services?

The NSW DNSPs consider that prescribing the existing negotiated distribution service principles diminishes their effectiveness and is inconsistent with the purpose of the negotiating framework.

Question 8

If the cost allocation principles are amended are the existing arrangements sufficient to enable compliance? Should transitional arrangements be considered to allow any rule changes to have effect as soon as possible?

The NSW DNSPs do not consider that transitional requirements are necessary, in the event that the cost allocation principles are amended.

²⁰ See clause 6.5.6(b)(2) and clause 6.5.7(b)(2) of the NER.

²¹ AER Electricity distribution network service providers – Cost allocation guidelines, June 2008, clause 5.2 and 5.3.

²² DNSPs will have to dedicate more time and resources maintaining a compliant CAM, while the AER will have to dedicate more time and resources to determining DNSP's CAM more frequently.

²³ Imposing onerous regulatory obligations will increase DNSP's compliance costs, which will ultimately be passed through to consumers in the form of higher electricity prices.