



5 February 2010

**Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235**

Submitted online at AEMC website www.aemc.gov.au

Subject: Draft Statement of Approach on Cost Recovery (EPR0018)

AGL welcomes this opportunity to comment on the Draft Statement of Approach (***Draft Statement***) issued by AEMC (***the Commission***) in response to a request for advice by the Ministerial Council on Energy (***MCE***) on cost recovery for mandated smart meter pilots, trials and roll-outs.

AGL believes the overall approach outlined in the ***Draft Statement*** is sound. AGL agrees with ***the Commission*** on the scope of advice that will consider the adequacy of existing National Electricity Rules (***Rules***) for cost recovery and possible alternative regulatory approach otherwise.

AGL supports the Commission's proposed decision process that includes the ***MCE*** policy principles issued in June 2008. In particular, AGL believes that the decision process should have a strong focus on a cost recovery framework that meets the ***MCE's*** requirement for future flexibility on contestability.

It is important to recognise that currently, the provision of smart meter services is a contestable service under the ***Rules***. Competition for the provision of smart meter services has been developing steadily since retail contestability, and has been effective for large customers. In recent years, more smart meters have been installed for smaller customers and this could be expected to increase as price caps are removed and the technology becomes more affordable.

By mandating the rollout of smart meters with a monopoly arrangement, the development of a competitive market for these services is likely to be impeded or delayed. In the long run, the interest of customer and energy retailing would be better served if a competitive market resumes sooner rather than later. AGL therefore believes that a regulatory framework for cost recovery should give due consideration for a return to contestable market by including active measures that promote competitive behaviours and reduces barriers to entry.

Another relevant issue in a cost recovery framework is the regulation of service performance outcomes. In a monopoly arrangement, the retailers have little influence over the quality of service delivery and would rely on regulatory compliance for corrective actions and incentives for improvements.

Section 3.5.3 of the ***Draft Statement*** suggests that there appears to be significant operational uncertainties and risks associated with a large scale rollout of smart meters and technology. AGL is concerned with how these risks are allocated and the potential knock-on effect on retailer cost and customer services due to performance failures.

- > Being selected as a member of the Dow Jones Sustainability Index 2006/07
- > Gaining accreditation under the National GreenPower Accreditation Program for AGL Green Energy®, AGL Green Living® and AGL Green Spirit
- > Being selected as a constituent of the FTSE4Good Index Series

In AGL's view, the choice of a regulatory framework for cost recovery should place significant emphasis on the accountability of service outcome and ensure the responsibility and risks for managing them is allocated to the mandated party who is best placed to manage them.



In terms of cost recovery, the retailers should be able to pass on the cost of pilot and trials to a mandated party as there is no other mechanism for the recovery of such costs in an equitable manner. Given that the pilots and trials are for public benefit, the cost should not be borne by a particular retailer participating in the trials. AGL agrees that the determination for a mandated rollout should clearly provide for the recovery of such cost by the retailers through the mandated party.

In AGL's view, the determination should also ensure a retailer is able to recover its cost of implementing the smart meter rollout. The retailers would be reluctant to introduce new product and services for smart meters if it is unable to recover the implementation cost. This could potentially compromise the realisation of benefits from the rollout of smart meters particularly on demand response.

AGL supports the Commission's view in the report that smart meter services are a "joint product". It highlights the fact that the realisation of the benefits is closely related to implementation by multiple participants including the retailers. Hence, the advice to **MCE** should duly recognise that the effectiveness of cost recovery regulatory framework for mandated parties is closely related to retailer's ability to recover its implementation cost for smart meter services.

AGL offers the following specific comments:

1. Alternative control service is preferred as smart meter services is distinct from the network services and is subject to a transition to a future contestable market. Hence, it is important that cost and charges related to smart meters rollout can be ring-fenced from the DUOS and network services. Furthermore, the charges for meter provision and service provision should be separated as these are currently two contestable markets.

This approach would greatly facilitate the resumption of contestability by providing a transparent disclosure of cost and charges for smart meters and services.

2. Alternative regulatory approaches should be considered. The existing approach appears to accommodate a relatively more predictable and stable investment in "poles and wires" which may not be "fit-for-purpose" for investment in technology and operation that is relatively new. An alternative approach that applies similar economic principles may be required to ensure the particular issues on the facilitation of future contestability, accountability for performance outcome and risk allocations can be effectively addressed.
3. The review of network tariff methodology would necessary include the recognition that unless retailer tariff is unregulated, it is difficult for cost reflective network charges to be passed through to end use customers. This issue demonstrates that while the TOR for the review is limited to cost recovery for mandated rollout, AGL believes that the advice to **MCE** should recognise the potential impact of external issues on the effective choice of a regulatory arrangement for cost recovery.

Please contact me if you have any further queries.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Alex Cruickshank'.

Alex Cruickshank
Head of Energy Regulation