



**Australian Energy Market Commission**

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## **CONSULTATION PAPER**

# **National Electricity Amendment (DNSP Recovery of Transmission-related Charges) Rule 2010**

### **Rule Proponent**

United Energy Distribution

2 September 2010

**RULE  
CHANGE**

This Consultation Paper has been prepared by the staff of the Australian Energy Market Commission (AEMC) to facilitate public consultation on the Rule change request. This Paper does not represent the views of the AEMC or any individual Commissioner of the AEMC.

Submissions due: 1 October 2010  
Reference: ERC0114

## **Inquiries**

Australian Energy Market Commission  
PO Box A2449  
Sydney South NSW 1235

E: [aemc@aemc.gov.au](mailto:aemc@aemc.gov.au)

T: (02) 8296 7800

F: (02) 8296 7899

Reference: ERC0114

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## **About the AEMC**

The Council of Australian Governments, through its Ministerial Council on Energy (MCE), established the Australian Energy Market Commission (AEMC) in July 2005 to be the rule maker for national energy markets. The AEMC is currently responsible for rules and providing advice to the MCE on matters relevant to the national energy markets. We are an independent, national body. Our key responsibilities are to consider rule change proposals, conduct energy market reviews and provide policy advice to the MCE as requested, or on AEMC initiative.

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# 1 Introduction

On 24 June 2010, the Australian Energy Market Commission (AEMC or Commission) received a Rule change request from United Energy Distribution (Proponent) on behalf of Victorian distribution network service providers (DNSPs) in relation to how DNSPs recover the charges for connection to, and use of, the transmission system, inter-DNSP payments and avoided transmission use of system (TUOS) payments to embedded generators.

Under clause 6.18.7 of the National Electricity Rules (NER), DNSPs may recover 'charges for transmission use of system services' by including these charges in their pricing proposals. The Proponent requests that these pricing provisions be amended such that the reference to 'transmission use of system services' is replaced with 'transmission services' and to also add the recovery of charges for inter-DNSP payments and avoided TUOS payments. The Proponent considers that the proposed Rule reflects the existing practice in Victoria and other jurisdictions. The Proponent also considers that the proposed Rule would remove uncertainty about how these charges should be recovered.

The Proponent also requests that the Rule change request be subject to the expedited Rule making process under section 96 of the National Electricity Law (NEL) on the grounds that the Rule change relates to a 'non-controversial Rule'.<sup>1</sup> The Commission has decided not to expedite this Rule change request.

This Consultation Paper has been prepared by the staff of the AEMC to facilitate public consultation on the Rule change request. This paper does not represent the views of the AEMC or any individual Commissioner of the AEMC.

This paper:

- sets out a summary of, and a background to, the Rule change request;
- identifies a number of questions and issues to facilitate the consultation on this Rule change request; and
- outlines the process for making submissions.

## Submissions

Submissions are to be received by 1 October 2010. Additional details on lodging a submission are outlined in Chapter 6 of this paper.

## Timetable

The draft Rule determination (and draft Rule if applicable) is required to be published by 2 December 2010.

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<sup>1</sup> A "non-controversial Rule" is defined under section 87 of the NEL and means "a Rule that is unlikely to have a significant effect on the national electricity market".

## 2 Background

This Chapter provides an overview of the current processes that DNSPs use to recover transmission service charges, inter-DNSP payments and avoided TUOS payments. It also provides background information on the revenue and pricing regulatory processes.

### Current processes and issue identified

DNSPs are currently subject to a five-year regulatory control period.<sup>2</sup> The Australian Energy Regulator (AER) makes distribution determinations giving consideration to the building blocks approach to determine the revenue that DNSPs are entitled to, including consideration of forecast operating expenditure (opex) which has to reasonably reflect efficient and prudent costs based on realistic estimates of forecast demand and cost inputs.<sup>3</sup>

Under the current NER, DNSPs are required to prepare annual pricing proposals, which set out the pricing structure they will use each year to recover the allowed revenues set out in the distribution determination.<sup>4</sup> In addition, the pricing process includes the recovery of charges incurred by DNSPs for 'transmission use of system services' and payments DNSPs make under feed-in schemes and climate change funds.<sup>5</sup> DNSPs must submit pricing proposals to the AER each year and the AER must approve them if they comply with the distribution determination and pricing provisions.<sup>6</sup>

This Rule change request raises the issue that there appears to be a lack of specificity under the pricing provisions in Chapter 6 of the NER, where the pricing provisions only refer to the pass through of 'transmission use of system' charges.<sup>7</sup> The Proponent proposes that charges for connection to, and use of, the transmission system, inter-DNSP payments and avoided TUOS payments to embedded generators should also be included in these provisions.

Examples of the magnitude of the charges that are relevant include:

- Integral Energy in New South Wales: approximately \$127m (actual) in 2008/09, \$171m (expected) in 2009/10 and \$207m (forecast) in 2010/11;<sup>8</sup>

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<sup>2</sup> Clause 6.3.2(b) of the NER.

<sup>3</sup> Clauses 6.4.3(a)(7) and 6.5.6(c) of the NER.

<sup>4</sup> Clause 6.18.2 of the NER.

<sup>5</sup> Clauses 6.18.2, 6.18.7 and 6.18.7A of the NER.

<sup>6</sup> Clauses 6.18.2 and 6.18.8 of the NER.

<sup>7</sup> Clause 6.18.7 of the NER.

<sup>8</sup> Integral Energy, Annual Pricing Proposal 2010/11, April 2010, p. 88. Note: These figures include transmission charges to be paid to transmission network service providers (TNSPs) and avoided TUOS payments.

- Country Energy in New South Wales: approximately \$250m (forecast) in 2010/11;<sup>9</sup>
- Energex in Queensland: approximately \$247m (actual) in 2008/09 and \$345m (forecast) in 2010/11;<sup>10</sup> and
- ETSA Utilities in South Australia: approximately \$189m (actual) in 2008/09, \$191m (expected) in 2009/10 and \$225m (forecast) in 2010/11.<sup>11</sup>

We note that these examples may not necessarily be reflective of the costs to Victorian DNSPs.

### **Previous Victorian DNSP revenue determinations**

The Essential Services Commission of Victoria (ESC) was previously responsible for the economic regulation of distribution revenue in Victoria. These ESC determinations allowed DNSPs to factor all charges for connection to, and use of, the transmission system, inter-DNSP payments and avoided TUOS payments to embedded generators into their tariff structures. In its Electricity Distribution Price Review for the regulatory control period 2006 to 2010, the ESC specified that the aggregate cost that DNSPs are allowed to recover through their transmission tariffs (the Maximum Transmission Revenue) includes transmission-related and other charges.<sup>12</sup>

### **Current Victorian DNSP revenue determination**

In June 2010, for the first distribution determination for Victoria to be made by the AER, the AER published its draft decision on the distribution determination for Victoria for the regulatory control period 2011 to 2015.<sup>13</sup> In its draft decision, the AER did not consider that transmission connection charges, inter-DNSP charges and avoided TUOS charges should be recovered under clause 6.18.7 of the pricing process, as this clause specifically refers to 'recovery of charges for transmission use of system services'.<sup>14</sup> The AER considered that these charges did not fall within the definition of

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<sup>9</sup> Country Energy, Annual Network Prices Report, 1 July 2010 - 30 June 2011, June 2010, p. 8. Note: This figure includes transmission charges to be paid to TNSPs, inter-DNSP payments and avoided TUOS payments.

<sup>10</sup> Energex, Pricing Proposal for the period 1 July 2010 - 30 June 2011, May 2010, p. 45. Note: The 2008/09 figure includes transmission charges to be paid to TNSPs and avoided TUOS payments. The 2010/11 figure includes transmission charges to be paid to TNSPs, inter-DNSP payments and avoided TUOS payments.

<sup>11</sup> ETSA Utilities, Pricing Proposal 2010-11, June 2010, p. 67. Note: These figures only include transmission charges to be paid to ElectraNet. The avoided TUOS payments to embedded generators are recouped by ETSA Utilities through the recovery mechanism for the TUOS charges.

<sup>12</sup> For instance, see: section 12.3.2 of ESC, Electricity Distribution Price Review 2006-10, Final Decision Volume 1, Statement of Purpose and Reasons, October 2005, pp. 476-477; clause 3.3.2 of ESC, Electricity Distribution Price Review 2006-10, Final Decision Volume 2, Price Determination, October 2005, p. 36; and ESC, Open letter to stakeholders and interested parties, Guidance on calculation of avoided TUOS payments, 19 October 2005.

<sup>13</sup> AER, Victorian Distribution determination 2011-15, Draft decision, June 2010.

<sup>14</sup> Ibid, pp. 64-66.

TUOS services under the NER as they are not related to the use of the transmission network.<sup>15</sup> The AER noted Victorian DNSPs intend to submit a Rule change request to the Commission to address this issue. The AER also indicated that it would consider the matter in its final decision, subject to the outcome of the Rule change process.

Following the AER's draft decision, the Proponent submitted this Rule change request which seeks to amend the pricing provisions so that transmission service charges, inter-DNSP payments and avoided TUOS payments can be incorporated in the DNSP's pricing proposal.

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15 Ibid.



### 3 Details of the Rule Change Request

The Rule change request from the Proponent proposes to:<sup>16</sup>

- address a lack of specificity under clauses 6.18.2 and 6.18.7 of the NER where the pricing provisions refer only to the pass through of 'transmission use of system' charges;
- amend clauses 6.18.2 and 6.18.7 by adding transmission service charges, inter-DNSP payments and avoided TUOS payments; and
- allow DNSPs to incorporate these charges in their annual pricing proposals.

In its Rule change request the Proponent provides its rationale for the Rule change request. A number of key points raised in the Rule change request are summarised as follows:

- transmission service charges, inter-DNSP payments and avoided TUOS payments are no different to charges for TUOS services which are currently allowed to be recovered under clause 6.18.7 of the NER. They are charges for services that are inputs to the provision of standard control services and should therefore be dealt with in a comparable fashion to charges for TUOS services in pricing proposals submitted by DNSPs;
- the proposed Rule merely gives effect to the intention of existing regulation and practice in Victoria for DNSPs to recover the aggregate of all charges for connection to, and use of, the transmission system, inter-DNSP payments and avoided TUOS payments in the form of transmission tariffs from all distribution customers;
- the proposed Rule merely codifies existing regulatory practice such as for the Queensland and New South Wales DNSPs who are able to recover transmission service charges, inter-DNSP payments and avoided TUOS payments;
- it is general practice for DNSPs to include charges for transmission services as part of TUOS service charges in their respective pricing proposals (as opposed to forecast costs associated with transmission service charges as a part of opex because it is not accepted regulatory practice); and
- the Rule change request addresses a gap in the NER and clarifies a drafting oversight.

The Rule change request includes a proposed Rule.

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<sup>16</sup> United Energy Distribution, Rule change request, 24 June 2010.

## 4 Assessment Framework

The Commission's assessment of this Rule change request must consider whether the proposed Rule promotes the National Electricity Objective (NEO) as set out under section 7 of the NEL. In assessing the Rule change request against the NEO the following issues will be taken into consideration:

- recovery of efficient costs – does the proposed Rule ensure that DNSPs would be able to recover appropriate costs and encourage efficient investment in, and operation of, distribution and transmission networks?
- regulatory certainty and transparency – does the proposed Rule provide an appropriate amount of regulatory certainty and transparency to reduce ambiguity and costs in regulating the recovery of transmission service charges, avoided TUOS payments and inter-DNSP payments?
- administrative efficiency – would the proposed Rule improve efficiency in administering how the relevant charges are recovered by DNSPs and what impact would these have on current arrangements for DNSPs?

The proposed Rule will be assessed against the relevant counterfactual arrangements, which in this case are the current provisions in the NER.

It is noted that although Victorian DNSPs proposed this Rule change request, any amendments to Chapter 6 of the NER would affect all DNSPs.

## 5 Issues for Consultation

Taking into consideration the assessment framework and potential requirements to implement the proposed Rule, a number of issues for consultation that appear to be relevant to this Rule change request are set out in this Chapter.

These issues outlined below are provided for guidance. Stakeholders are encouraged to comment on these issues as well as any other aspect of the Rule change request or this paper including the proposed framework.

### 5.1 What charges should be recoverable?

The Rule change request proposes that charges for transmission services, inter-DNSP payments and avoided TUOS payments would be recovered as a pass through under the pricing process. In assessing this Rule change request, whether and how to define costs that are being considered should be analysed:

- Should the current definition for 'transmission services' under the NER apply?<sup>17</sup> If so, what would be 'charges' for transmission services? Should these charges only include charges for prescribed transmission services that transmission network service providers (TNSPs) impose on DNSPs (that is, the prescribed exit charge, the prescribed TUOS charge, and the prescribed common charge, which are determined under Chapter 6A of the NER)?
- As connection services are defined under the NER as prescribed transmission services, do charges for prescribed transmission services capture all connection costs?
- Are there other transmission-related charges that DNSPs incur in providing standard control services?
- How should 'inter-DNSP payments' be defined?
- Are there any other charges that should be included?

In considering the definition of the costs to be recovered, consideration must also be given to the appropriate level of prescription under the pricing process. If the framework is overly prescribed, it may present a risk that any legitimate costs may be unintentionally excluded; whereas if the framework was too broad, it may lead to inappropriate costs being recovered:

- What factors should be considered in order to establish the appropriate level of prescription in defining the relevant charges?

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<sup>17</sup> 'Transmission services' is defined in Chapter 10 of the NER as: 'The services provided by means of, or in connection with, a transmission system'.

- What level of transparency would be appropriate of how transmission service charges, avoided TUOS payments and inter-DNSP payments are calculated?<sup>18</sup>

## 5.2 How should the charges be recovered?

The revenue and pricing principles state that the DNSP should be provided with a reasonable opportunity to recover at least the efficient costs that it incurs in providing direct control network services and complying with a regulatory obligation or requirement or making a regulatory payment. In the absence of an ability to recover costs, DNSPs would reduce the amount of investment into the provision of distribution services.

Under the current NER, the following avenues are available to DNSPs under which they may recover costs through:

- (i) the five-yearly distribution determination process where the AER determines a maximum allowed revenue;
- (ii) applying to the AER for a cost pass through for any unforeseen events outside the DNSP's control;<sup>19</sup> and
- (iii) including other permitted charges directly under the pricing process – that is, charges for TUOS services and payments for feed-in schemes and climate change funds.<sup>20</sup>

That is, costs under the distribution determination process are subject to rigorous economic assessments, which includes examining the types, and efficiency, of costs incurred by DNSPs to ensure these costs meet regulatory requirements. However, the pricing process provides less rigour and charges that are passed through directly under the pricing process would generally relate to costs that are outside the control of DNSPs (or charges that are subject to regulatory oversight under other processes).

The Rule change request raises the following questions:

- Are charges for 'transmission services', inter-DNSP payments and avoided TUOS payments outside the control of DNSPs (or subject to other regulatory oversight)?
- If DNSPs have some control over the level of these costs, would including these costs to be passed through directly under the pricing process provide sufficient incentive to ensure that these costs are minimised?
- Should any of these costs be included in the distribution determination process?

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<sup>18</sup> 'Avoided TUOS payments' are referred to as 'avoided charges for the locational component of prescribed TUOS services' and defined under rule 5.5(h) of the NER.

<sup>19</sup> Clause 6.6.1 of the NER.

<sup>20</sup> Clauses 6.18.7 and 6.18.7A of the NER.

### **5.3 How to ensure administrative efficiency?**

The distribution determination and pricing provision processes require the AER and DNSPs to undertake a number of administrative steps to ensure that the provisions under the NER are met:

- What factors should be taken into consideration to ensure that any amendments to the revenue determination and pricing process minimises the administrative costs of the AER and DNSPs?

### **5.4 What savings and transitional requirements would be required?**

We note that the AER's draft distribution determination for Victoria for the regulatory control period 2011 to 2015 will be published in October 2010. Given that this Rule change process will not be completed before October, if a Rule were to be made, savings and transitional arrangements would likely be required to allow any Rule made to be applied as soon as practicable. The savings and transitional provisions would also need to take into account distribution determinations and pricing proposals that are already in place. To minimise the risk of 'double counting', the recovery of any charges under any new provisions should not be additional to recovery under existing provisions.

## **6 Lodging a Submission**

The Commission has published a notice under section 95 of the NEL for this Rule change request inviting written submission. Submissions are to be lodged online or by mail by 1 October 2010 in accordance with the following requirements.

Where practicable, submissions should be prepared in accordance with the Commission's Guidelines for making written submissions on Rule change requests.<sup>21</sup> The Commission publishes all submissions on its website subject to a claim of confidentiality.

All enquiries on this project should be addressed to Charles Hoang on (02) 8296 7800.

### **6.1 Lodging a submission electronically**

Electronic submissions must be lodged online via the Commission's website, [www.aemc.gov.au](http://www.aemc.gov.au), using the "lodge a submission" function and selecting the project reference code "ERC0114". The submission must be on letterhead (if submitted on behalf of an organisation), signed and dated.

Upon receipt of the electronic submission, the Commission will issue a confirmation email. If this confirmation email is not received within 3 business days, it is the submitter's responsibility to ensure the submission has been delivered successfully.

### **6.2 Lodging a submission by mail**

The submission must be on letterhead (if submitted on behalf of an organisation), signed and dated. The submission should be sent by mail to:

Australian Energy Market Commission  
PO Box A2449  
Sydney South NSW 1235

Or by Fax to (02) 8296 7899.

The envelope must be clearly marked with the project reference code: "ERC0114".

Except in circumstances where the submission has been received electronically, upon receipt of the hardcopy submission the Commission will issue a confirmation letter.

If this confirmation letter is not received within 3 business days, it is the submitter's responsibility to ensure successful delivery of the submission has occurred.

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<sup>21</sup> This guideline is available on the Commission's website.

## Abbreviations

AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
Commission	See AEMC
DNSP	distribution network service provider
ESC	Essential Services Commission of Victoria
NEL	National Electricity Law
NEO	National Electricity Objective
NER	National Electricity Rules
opex	operating expenditure
TNSP	transmission network service provider
TUOS	transmission use of system